



COMMONWEALTH
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Climate
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Initiative

Primer on Climate Change: Directors' Duties and Disclosure Obligations

In support of the Principles for Effective Climate Governance

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In collaboration with



Canada Climate
Law Initiative

L'Initiative canadienne
de droit climatique

In collaboration with



Oxford Sustainable Finance Programme

Smith School of Enterprise and the Environment
University of Oxford
South Parks Road
Oxford, OX1 3QY
United Kingdom

Email:
info@commonwealthclimatelaw.org

Climate Governance Initiative

Climate Governance Initiative
In collaboration with the World Economic Forum

Email:
info@climate-governance.org



Canada Climate Law Initiative

Peter A. Allard School of Law
University of British Columbia
1822 E Mall
Vancouver, BC
V6T 1Z1
Canada

Email: ccli-info@allard.ubc.ca



Primer on Climate Change:

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Executive Summary

The evolution of our understanding of climate change from an ethical or environmental issue to one that presents foreseeable financial and systemic risks (and opportunities) over short, medium and long-term investment horizons has significantly changed its relevance to the governance of both corporations and investors. This evolution means there are serious implications for the duties of directors and officers, and potential disclosure obligations for companies.

This Primer provides an overview of contemporary evidence that climate change presents foreseeable, and in many cases material, financial and systemic risks that affect corporations and their investors. It then discusses: (1) general climate obligations in the jurisdictions where The Climate Governance Initiative is present through its global network of national Chapters; (2) how company law and directors' duties in these jurisdictions require directors to incorporate climate change into their strategies, legal oversight, and supervision of the companies entrusted to their care; (3) disclosure obligations; and then (4) advice to directors.

Litigation challenging companies' contributions to climate change is becoming a reality in many countries. Over fifteen hundred cases have been filed as of the end of 2020 to recoup some of the damage caused by climate change or the costs of adaptation, or to challenge governments' or corporations' actions or failure to act. Challenges to the actions—and inactions—of directors are starting to accumulate, evidenced in stark form by the judgment in the Netherlands on 26 May 2021, ordering Royal Dutch Shell to reduce its CO₂ emissions by 45% from 2019 levels by the end of 2030. We have produced this Primer for board directors so they can be informed and prudent advocates, encouraging their boards to take up the issue of climate change in the development of their companies' corporate strategy, oversight, and disclosure. This, alone, is the most effective thing directors can do to fulfil their obligation to their companies while steering well clear of any personal liability exposure from the potential increase of litigation.

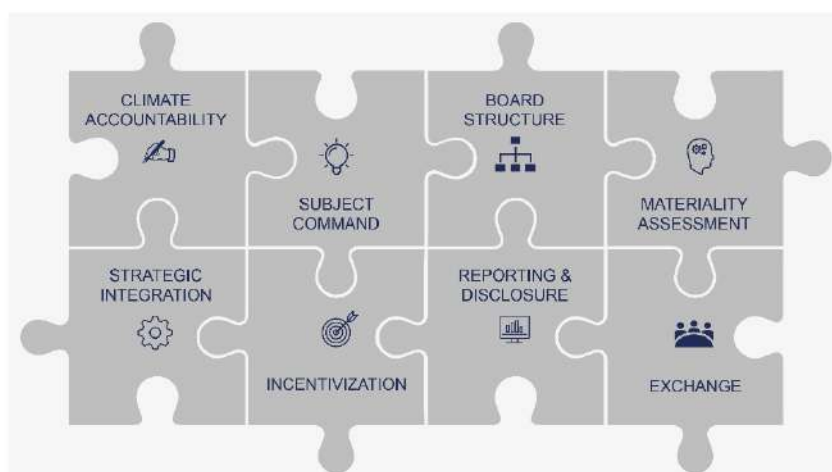
Foreword



Climate change poses an existential risk to humanity, the planet and the global economy on a scale never before seen. This is prompting governments and businesses around the world to take serious action to accelerate the transition to a new economic model that delivers on the commitments taken in the COP21 Paris Agreement signed in 2015. Doing so means recalibrating all economic activity to achieve net-zero greenhouse gas emissions by 2050 or earlier, consistent with an average temperature rise above the pre-industrial age of no more than 1.5°C. It also requires a wholesale shift in how companies are governed: for board directors, it means placing the climate transition at the heart of corporate strategy, ensuring that board decision-making processes properly embed climate considerations.

However, despite this growing awareness of the scale and urgency of the climate crisis, few directors possess the specific interdisciplinary skills necessary to effect this wholesale change of culture and behaviour. It is for this very reason that the Climate Governance Initiative (CGI) came into being: in 2019, the World Economic Forum unveiled the [Principles for Effective Climate Governance](#), a comprehensive set of guidance principles that lay out best practice for boards and their directors in respect of the climate. To facilitate their promotion and implementation, local CGI “Chapters” have been set up around the world to serve as centres of expertise and venues for directors to exchange with each other as well as with a wide range of subject matter experts.

Figure : Guiding principles for effective climate governance on corporate boards



The first of these eight CGI Principles, entitled “Climate accountability on boards”, concerns an issue that has frequently stood in the way of board directors factoring climate concerns into their decisions: how their legal duties and obligations apply in the context of the now-universal recognition of the extreme threat that climate change poses to the global economy and therefore to individual businesses. Too often, boards are concerned that “leaving profitable business on the table”, or acting according to “how we wish the world to be, rather than how it is” will place them in breach of their legal obligations to shareholders, or worse, result in litigation or removal. This Primer tackles precisely this issue, and provides a succinct, easily accessible summary that non-lawyers who serve on boards can readily understand and act on. It will serve as a valuable resource to the global network of CGI Chapters, and enable directors around the world to act in a fully-informed manner on their legal obligations as they confront this historic challenge.

The Climate Governance Initiative currently has 14 active Chapters in Brazil, Brussels, Canada, Chile, France, Germany, Italy, Malaysia, the Nordic region, Poland, Russia, Switzerland, the United Kingdom and the United States. Additional Chapters in Australasia, Europe, Africa and Latin America are currently in formation, bringing the total to some 25 national and regional members by the end of 2021.

Karina Litvack
Chairman, Climate Governance Initiative

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- Karina Litvack, Climate Governance Initiative
- Prof. Cynthia Williams, Professor of Law, York University, Canada Climate Law Initiative, CCLI
- Ellie Mulholland, CCLI, MinterEllison
- Dr. Sabrina Bruno, Full Professor of Comparative Corporate Law, University of Calabria, Chapter Zero Italy: The Nedcommunity Climate Forum
- Dr. Janis Sarra, Professor of Law, University of British Columbia, Canada Climate Law Initiative, CCLI
- Sarah Barker, MinterEllison, CCLI
- Dr. Ernest Lim, Associate Professor of Law, National University of Singapore, CCLI
- Dr. Umakanth Varottil, Associate Professor of Law, National University of Singapore, CCLI
- Sonia li Trottier, Canada Climate Law Initiative
- Alice Maxwell, CCLI
- Nick Young, CCLI
- Julie Luanco, CCLI
- Alex Cooper, CCLI

Contributors to the jurisdictional overviews

- Lina Pimentel Garcia, Mattos Filho Brazil
- Tábata Boccanera Guerra de Oliveira, Mattos Filho Brazil
- Franco Acchiardo, Grasty Quintana Majlis Chile
- Blanche Balian, BakerMcKenzie France
- Clotilde Guyot-Rechard, BakerMcKenzie France
- Guillaume Nataf, BakerMcKenzie France
- Dr. Henning Schaloske, Clyde & Co Germany
- Dr. Masafumi Nakahigashi, Professor of Law, Nagoya University, Japan
- Dr. Yoshihiro Yamada, Professor of Law, Ritsumeikan University, Japan
- To' Puan Janet Looi, SKRINE Malaysia
- Francine Ariel Paul, SKRINE Malaysia

- Juan Pablo Sainz M., Nader, Hayaux & Goebel Mexico
- Yves Hayaux du Tilly L., Nader, Hayaux & Goebel Mexico
- Nikita Shabalin, DLA Piper Russia
- Corinne Nacht, Baker McKenzie Switzerland
- Philippe Reich, Baker McKenzie Switzerland
- Kateryna Soroka, DLA Piper Ukraine
- Oleksandr Kurdydyk, DLA Piper Ukraine

About the Climate Governance Initiative

The Climate Governance Initiative (CGI)'s primary aim is to educate and equip non-executive directors with the skills and knowledge necessary to address climate change at the board level, and mobilise them to serve as advocates for the adoption of a Paris-aligned climate transition strategy. It does so by supporting the establishment of national and regional hubs, known as Chapters, around the world that serve as venues for directors to exchange with and learn from peers, experts and key stakeholders. The core mission of the Chapters is to promote the implementation of the [Principles for Effective Climate Governance](#) published by the World Economic Forum in 2019.

About the Commonwealth Climate and Law Initiative

The Commonwealth Climate and Law Initiative (CCLI) is a legal research and stakeholder engagement initiative founded by the Oxford University Smith School of Enterprise and the Environment, ClientEarth, and Accounting for Sustainability (A4S). The CCLI examines the legal basis for directors and trustees to understand, manage, and report on climate change-related risk and climate mitigation. Its research is at the forefront of the intersection of climate and biodiversity risks under existing companies and securities laws. Founded to focus on four Commonwealth countries – Australia, Canada, South Africa, and the United Kingdom – the CCLI has expanded its remit to the United States, Hong Kong, India, Singapore, Japan, and Malaysia. The CCLI leverages the inter-disciplinary and cross-jurisdictional perspectives provided by its global experts from academia and the legal, accountancy, business, and scientific communities.

About the Canada Climate Law Initiative

The Canada Climate Law Initiative examines the legal basis for corporate directors, officers, pension fiduciaries, and asset managers to consider, manage, and report on climate-related financial risks and opportunities, advancing knowledge on effective climate governance practice and

exploring the scope and limits of fiduciary obligation in respect of climate change. It is a collaboration of the University of British Columbia (UBC) Centre for Business Law and Osgoode Hall Law School, York University; and is the Canadian partner of the global Commonwealth Climate and Law Initiative.

Disclaimer

Any errors or omissions in this briefing paper are the authors' own. The paper reflects the law as at June 2021.

The Climate Governance Initiative, the Commonwealth Climate and Law Initiative, the Canada Climate Law Initiative, their partner organisations and collaborators make no representations and provide no warranties in relation to any aspect of this publication, including regarding the liability of any individual person or entity or the advisability of investing in any particular company or investment fund or other vehicle. While we have obtained information believed to be reliable, we shall not be liable for any claims or losses of any nature in connection with information contained in this document, including but not limited to, lost profits or punitive or consequential damages.

The information contained in this Primer is of a general nature and it should not be relied upon as legal advice. Board directors should seek legal advice on the unique circumstances of their company and jurisdiction.

List of abbreviations

A4S: Accounting for Sustainability
AFORES: Retirement Funds Administrators of Mexico (*Administradoras de Fondos Para el Retiro*)
AktG: Stock Corporation Act
APRA: Australian Prudential Regulation Authority
ASIC: Australian Securities and Investments Commission
ASX: Australian Securities Exchange
BaFin: German Federal Financial Supervisory Authority
BNDES: Social and Economic Development Bank of Brazil (*Banco Nacional do Desenvolvimento Econômico e Social*)
BNM: Bank Negara Malaysia
BRR: Business Responsibility Reporting
BRSRs: Business Responsibility and Sustainability Reports
CA: Companies Act
CCLI: Commonwealth Climate and Law Initiative
CDP: Carbon Disclosure Project
CEO: Chief Executive Officer
CGI: Climate Governance Initiative
CMF: Financial Markets Commission of Chile (*Comisión para el Mercado Financiero*)
CO: Swiss Code of Obligations
CO₂: Carbon Dioxide
COD: Proposal N.2021/0104 or Corporate Sustainability Reporting Directive Proposal, EU
COP21: 2015 United Nations Climate Change Conference
CPG 229: Prudential Practice Guide CPG 229 Climate Change Financial Risks
CRISA: Code for Responsible Investing in South Africa
CSA: Canadian Securities Administrators
CSR: German Council for Sustainable Development
CSRD: Corporate Sustainability Reporting Directive
CVM: Securities and Exchange Commission of Brazil (*Comissão de Valores Mobiliários*)
DCGK: German Corporate Governance Code (*Deutscher Corporate Governance Kodex*)
DPEF: French Extra-Financial Performance Report (*Déclaration de Performance Extra-Financière*)
ECB: European Central Bank
EQA 1974: Environmental Quality Act
ESG: environmental, social, and corporate governance
EU: European Union
F4GBM Index: FTSE4Good Bursa Malaysia Index
FCA: Financial Conduct Authority
FIEA: Japanese Financial Instruments and Exchange Act
FINMA: Swiss Financial Market Supervisory Authority
FRC: Financial Reporting Council

FSOC: U.S. Financial Stability Oversight Council
GHG: greenhouse gas
GmbHG: German Act on Limited Liability Companies (*Gesetz betreffend die Gesellschaften mit beschränkter Haftung*)
GRI: Global Reporting Initiative
HGB: German Commercial Code (*Handelsgesetzbuch*)
HKEX: Hong Kong Stock Exchange
HKMA: Hong Kong Monetary Authority
ICDR: Issue of Capital and Disclosure Requirements
IEA: International Energy Agency
IFRS: International Financial Reporting Standards
IIRC: International Council on Integrated Reporting
IOSCO: International Organization of Securities Commissions
ISE B3: Corporate Sustainability Index (*Índice de Sustentabilidade Empresarial*)
JC3: Joint Committee on Climate Change
MAS: Monetary Authority of Singapore
MCCG: Malaysian Code on Corporate Governance
MD&A: Management discussion and analysis
MESTECC: Ministry of Energy, Science, Technology, Environment and Climate Change
MEWA: Ministry of Environment and Water
NGFS: Network of Central Banks and Supervisors for Greening the Financial System
NZE2050: The Net-Zero Emissions by 2050 scenario released by the IEA in May 2021
OECD: Organisation for Economic Co-operation and Development
OMB: U.S. Office of Management and Budget
OSFI: Office of the Superintendent of Financial Institutions
PACTE: French Action Plan for Business Growth and Transformation (*Plan d'Action pour la Croissance et la Transformation des Entreprises*)
PACTT: Prudential Authority Climate Think Tank
PLC: Publicly-listed Company
RBA: Reserve Bank of Australia
RG: Regulatory Guide
SASB: Sustainability Accounting Standards Board
SC: Securities Commission Malaysia
SC Guidelines: Guidelines on Conduct of Directors of Listed Corporations and their Subsidiaries, Securities Commission Malaysia
SEBI: Securities & Exchange Board of India
SEC: U.S. Securities and Exchange Commission
SFB: Sustainable Finance Committee of German Federal Government
SFC: Hong Kong Securities and Future Commission
SFDR: Sustainable Finance Disclosure Regulation
SOC: Say on Climate
SNB: Swiss National Bank
SREP: Supervisory Review and Evaluation Process, EU
STAGE: Hong Kong Sustainable and Green Exchange

TCFD: Task Force on Climate-related Financial Disclosures

TEG: Technical expert group on sustainable finance, EU

UBC: University of British Columbia

WEF: World Economic Forum



1. Climate Change as a Financial and Systemic Risk

1. Climate Change as a Financial and Systemic Risk

The links between climate change and financial risk are becoming increasingly evident and inextricable. Our understanding of climate change has evolved from a purely “ethical issue” or “environmental externality” to an issue that poses foreseeable financial risks and opportunities for companies across short, medium and long-term horizons.

The scale and speed of climate change risks and opportunities in the transition to a zero-carbon economy received heightened attention in May 2021 with the long-anticipated release of the International Energy Agency (IEA)'s first-ever attempt to model a feasible pathway to net-zero GHG emissions by 2050 (NZE2050). The NZE2050 Scenario lays out a comprehensive set of measures that need to be taken across the whole of the global economy in order to deliver on this net-zero goal; these include significant changes in energy generation, transport, infrastructure and the built environment by 2030, including an immediate stop on all new fossil fuel exploration and development,¹ and consequently a major reordering in the geographic concentration of fossil fuel production to a handful of low-cost producing countries.

The implications of the NZE2050 Scenario for companies in the industry sectors facing either accelerated decline or rapid growth are momentous. Companies facing structural decline can expect heightened pressure from investors to stress-test their businesses against these new data, and to demonstrate their ability to remain resilient in the face of uncertainty regarding the pace of change, failing which access to capital will continue to suffer headwinds. For directors, this adds yet another tool they must use in the boardroom when modelling risk and strategic options.

According to the 2017 recommendations of the [Task Force on Climate-related Financial Disclosures](#) (TCFD), climate change is one of the most significant and complex risks facing organisations.² The widespread support for the TCFD recommendations reflects the growing consensus among the business, financial and regulatory communities of the financial and systemic risks presented by climate change and of the necessity of embedding climate change in financial risk management, disclosure and supervisory practices.³

¹ IEA, 'Net Zero by 2050: A Roadmap for the Global Energy Sector' (May 2021) 20-21 <<https://www.iea.org/reports/net-zero-by-2050>>.

² TCFD, 'Final Report: Recommendations of the Task Force on Climate-related Financial Disclosures' (June 2017), ii. <<https://www.fsb-tcf.org/publications/final-recommendations-report/>>.

³ *Ibid*, 5-6; Mercer, 'Investing in a time of climate change' (2015): <<https://www.mercer.com.au/content/dam/mercer/attachments/asia-pacific/australia/investment/sustainable-growth/mercer-climate-change-study-2015.pdf>>.



Figure 1: Climate-related financial risks to entities. Source: TCFD Final Recommendations (2017) p. 8.

In 2018, the Bank of England Prudential Regulation Authority explained that these financial risks have distinctive elements. The risks are far-reaching in breadth and magnitude across the economy, involve uncertain and extended time horizons, are foreseeable, and – crucially – the magnitude of future financial risks depends in large part on decisions taken today.⁴

Moving beyond company-specific financial risks, climate change is now recognised as a systemic risk. This was made clear in 2019 by [The Network of Central Banks and Supervisors for Greening the Financial System](#) (NGFS), a global coalition of over 90 central banks and supervisors, in its first comprehensive report, [A Call to Action](#), which stated:

Climate-related risks are a source of financial risk. It is therefore within the mandates of central banks and supervisors to ensure the financial system is resilient to these risks.⁵

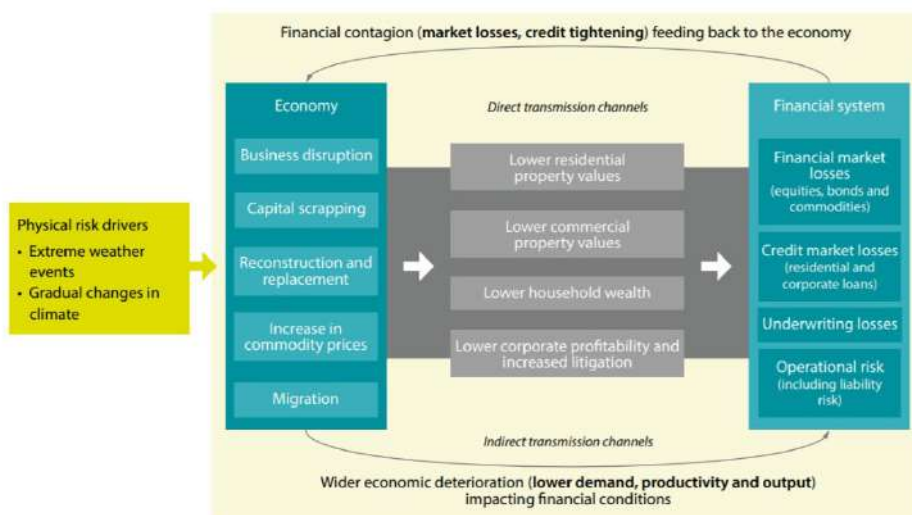
According to the Banque de France and the Bank for International Settlements, known as the 'central bank of central banks', the radical uncertainty of climate change and society's responses to it mean that

⁴ Bank of England Prudential Regulation Authority, *Transition in Thinking: The impact of climate change on the UK banking sector* (September 2018) <<https://www.bankofengland.co.uk/prudential-regulation/publication/2018/transition-in-thinking-the-impact-of-climate-change-on-the-uk-banking-sector>>.

⁵ NGFS, 'A Call for Action: Climate Change as a Source of Financial Risk' (April 2019), 4 <https://www.banque-france.fr/sites/default/files/media/2019/04/17/ngfs_first_comprehensive_report_-_17042019_0.pdf>.

climate change poses 'green swan' systemic risks that could lead to a financial crisis.⁶

From physical risk to financial stability risks



From transition risk to financial stability risks



Figure 2: Climate-related systemic risks arising from transition risks. Source: NGFS Guide for Supervisors: Integrating climate-related and environmental risks into prudential supervision (2020) p. 13.

As businesses become visibly disrupted from the impacts of a changing climate and the transition to a net-zero emissions economy, the awareness of these financial and systemic risks has become squarely mainstream. In

⁶ Bank of International Settlements and Banque du France, The green swan - Central banking and financial stability in the age of climate change (January 2020) <<https://www.bis.org/publ/othp31.pdf>>.

2021, even in light of the pandemic, the World Economic Forum's (WEF) [Global Risks Report](#) identified climate change and related environmental issues as four of the five most likely risks to the global economy, according to WEF's surveys of global executives, with infectious disease joining climate risks within the five most likely risks.⁷ Two of the climate risks that board members find likely are particularly acute: climate action failures by governments, and human-made environmental damage.

As a now widely-recognised financial and systemic risk, as well as a factor that is integral to value creation, climate change squarely engages directors' duties and disclosure obligations. In line with these developments, financial regulators have increasingly insisted on effective climate risk disclosure and governance.⁸ So, too, investors have set normative expectations of director conduct and are becoming increasingly vocal in communicating these expectations in their voting and stewardship activities.⁹

The 2021 proxy season revealed a marked acceleration in the way investors expected to hold companies accountable for their climate strategies. In Europe, the U.S., Asia and Australia, this took the form of so-called Say On Climate (SOC) proposals, whereby investors tested the limits of local law¹⁰ by urging boards to put their climate transition plans to an annual advisory shareholder vote. Many companies voluntarily did so, while in other cases, including in the U.S., the focus was mainly on shareholder proposals demanding greater disclosure of greenhouse gas emissions and more ambitious and comprehensive target-setting. Against the backdrop of a newly-sympathetic U.S. Securities and Exchange Commission, which reversed its predecessor's approach by admitting rather than systematically disallowing shareholder proposals on climate change, investors had much easier access to the ballot, and delivered some very stark messages.¹¹ But

⁷ WEF, 'Global Risks Report 2021 (2021)' <<https://reports.weforum.org/global-risks-report-2021/executive-summary/>>.

⁸ See TCFD, 'Final Report: Recommendations of the Task Force on Climate-Related Financial Disclosures' (2017) 5-6: <<https://www.fsb-tcf.org/wp-content/uploads/2017/06/FINAL-2017-TCFD-Report-11052018.pdf>>; Mercer, 'Investing in a time of climate change' (2015): <<https://www.mercer.com.au/content/dam/merceraustralia/attachments/asia-pacific/australia/investment/sustainable-growth/merceraustralia-climate-change-study-2015.pdf>>

⁹ See, e.g., BlackRock, Larry Fink's 2021 Letter to CEOs (January 2021) <<https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter>>.

¹⁰ In Italy, companies declined to act voluntarily on Say On Climate, citing limitations under the Civil Code regarding the areas on which the shareholders' assembly board may opine, and reasoning that climate strategy falls within the exclusive purview of the board, consistent with its responsibilities regarding the definition of corporate strategy. Companies in other Civil Law jurisdictions across Europe took the opposite view, as illustrated by the SOC proposals presented by including Glencore, Nestlé, Royal Dutch Shell, Total and Unilever, all of which passed with strong investor support. In the U.S. and Australia, Moody's and Rio Tinto committed to adopting a SOC vote, and the campaign to make this a regular feature of the proxy ballot continues.

¹¹ Among shareholder resolutions proceeding to vote in the U.S. were resolutions proposing that:

- ConocoPhillips and Chevron set and report on emission reduction targets covering the greenhouse gas emissions of the company's operations as well as their energy products (Scope 1, 2 and 3) (with 59.3% and 60.7% of the vote, respectively);
- Chevron report on the implications of the International Energy Agency's October 2020 Net Zero 2050 scenario (failed with 47.8% of the vote);
- Phillips 66 set and report on GHG reductions targets as well as the alignment of its lobbying activities with the objectives of the Paris Agreement (passed with 80.28% of the vote);

in a season of surprises, perhaps the greatest was the proxy fight initiated against ExxonMobil by a tiny hedge fund, which put four alternative candidates up for election to the board. Investors large and small responded with sufficient votes to hand a victory to three of the nominees, in an unprecedented move to use the ballot box to force strategic change on climate issues at one of the U.S.'s largest companies.

-
- General Electric evaluate and disclose if and how the company has met the criteria of the 'Net Zero Indicator' produced by the Climate Action 100+ (passed with 97.97% of the vote);
 - Exxon Mobil evaluates and reports on the alignment of its lobbying activities with the objectives of the Paris Agreement, on the basis that "corporate lobbying that is inconsistent with the goals of the Paris Agreement presents regulatory, reputational and legal risks to investors" (passed with 63.8 % of the vote).



2. Directors' Duties and Climate Change

2. Directors' Duties and Climate Change

Directors act as fiduciaries of the company in discharging their functions: overseeing corporate performance, strategy, and risk management; ensuring robust legal compliance systems are in effect in the company; approving significant transactions; and approving corporate reporting and disclosure.

As fiduciaries, directors owe two core duties to the company: **the duty of loyalty** and **the duty of care and diligence**. The precise nature and contours of these duties vary by jurisdiction. In common law jurisdictions, directors' fiduciary duties are articulated in statutes and in the case law, as developed over time by courts. In civil law jurisdictions, these duties are set out in statutory provisions that govern the conduct of directors.

While subject to variation across jurisdictions, the overarching concepts of loyalty and care in corporate governance are widespread. In general terms, the duty of loyalty requires that directors act honestly and in good faith in the best interests of the company, typically defined in exclusively financial terms. The duty of care requires that directors exercise reasonable care, skill, and diligence in the discharge of their stewardship functions, including by taking reasonable precautions against reasonably foreseeable harms.

What these duties require as a matter of good governance and prudent risk management is constantly evolving, in line with changes in the factual context in which directors act, knowledge of foreseeable risks, changes in regulations and market practices. A reasonable decision for a director fifty, ten or even five years ago might not look so reasonable today. Understanding these duties in the context of a changing external context is particularly relevant in the case of climate change, where the evidence of climate-related risks and opportunities is becoming ever more apparent, and changes in regulation are gathering momentum such that the likelihood of a disorderly and disruptive transition increases.

To discharge their duties, therefore, directors must integrate climate risks and opportunities into their governance roles.

3. Directors' Disclosure Obligations and Climate Change

Public companies in most jurisdictions have existing obligations under national laws to assess, manage, and report on financially-material climate risks. While jurisdictional specificities exist, corporate reporting and securities law frameworks generally require listed companies to disclose information that is materially relevant to their financial performance and prospects in narrative reports and financial statements.

A materiality requirement also covers disclosures in the financial statements. In November 2019, International Accounting Standards Board member Nick Anderson explained how climate risks fall within the existing principles-based requirements under International Financial Reporting Standards (IFRS):

Climate-related risks and other emerging risks are predominantly discussed outside the financial statements. However, as set out in [IFRS Practice Statement 2] *Making Materiality Judgements*, qualitative external factors, such as the industry in which the company operates, and investor expectations may make some risks 'material' and may warrant disclosures in financial statements, regardless of their numerical impact.¹²

In November 2020, the IFRS Foundation published guidance titled the *Effects of climate-related matters on financial statements*, which states that material climate-related financial information should be reported under IAS 1 Presentation of Financial Statements, IAS 2 Inventories, IAS 12 Income Taxes, IAS 16 Property, Plant and Equipment, IAS 38 Intangible Assets, IAS 36 Impairment of Assets, IAS 37 Provisions, Contingent Liabilities and Contingent Assets, IFRS 7 Financial Instruments: Disclosures, IFRS 9 Financial Instruments, and IFRS 13 Fair Value Measurement; and, in addition to this specific disclosure, that companies whose financial position or financial performance is particularly affected by climate-related matters must provide overarching disclosure.¹³

In addition to these mandatory disclosures, and requirements for principles-based narrative and financial statement disclosures, investors and regulators are increasingly calling for specific climate-related financial disclosures in the financial filings, in line with the TCFD recommendations. The TCFD 2020 Status Report issued in October 2020 states that the TCFD reporting framework has been endorsed by "over 1,500 organizations globally, including over 1,340 companies with a market capitalization of US\$12.6 trillion and financial institutions responsible for assets of \$150

¹² Nick Anderson, 'IFRS Standards and climate-related disclosures, In Brief' (November 2019), 3 <<https://www.ifrs.org/news-and-events/2019/11/nick-anderson-ifrs-standards-and-climate-related-disclosures/>>.

¹³ IFRS, 'Effects of climate-related matters on financial statements', (20 November 2020), 1, <<https://cdn.ifrs.org/-/media/feature/supporting-implementation/documents/effects-of-climate-related-matters-on-financial-statements.pdf?la=en>>.

trillion.”¹⁴ In 2021, BlackRock, an investor with \$8.67 trillion assets under management,¹⁵ called on investee companies to disclose a plan for how their business model will be compatible with a net-zero economy, to state how this plan is incorporated into the company’s long-term strategy, and to confirm that it has been reviewed by the board of directors.¹⁶ These disclosure requests are in addition to BlackRock’s 2020 policies that ask its investee companies to report in alignment with the TCFD recommendations and the Sustainability Accounting Standards Board (SASB).¹⁷

These climate-related disclosure standards have significant consequences for boards. Directors have obligations to approve or attest to the accuracy and completeness of disclosures made in financial filings. Directors on audit committees will likewise have additional responsibilities to engage in testing and overseeing the robustness of the climate scenario assumptions underpinning key aspects of the audit process.¹⁸

While some directors may be concerned about liability exposure from making disclosures in accordance with the TCFD reporting framework, a 2017 report by the CCLI explained how such concerns are misplaced:

It is true that under some disclosure regimes, directors may be primarily liable where they are involved in misleading disclosures by their company. In others, liability may be accessorial (i.e., to that of the company), or as an adjunct of the directors’ duties to exercise due care and diligence in the best interests of their company. However, this concern about liability exposure both misunderstands the nature of the TCFD recommendations and potentially misrepresents the application of securities disclosure laws in many jurisdictions.¹⁹

Simply put, disclosure in accordance with the TCFD recommendations could in fact be used as a strategy to ensure compliance with directors’ duties and disclosure obligations:

¹⁴ TCFD, *2020 Status Report: Taskforce on Climate-related Financial Disclosures*, (29 October 2020), 2 <<https://www.fsb.org/2020/10/2020-status-report-task-force-on-climate-related-financial-disclosures/>> (hereafter TCFD 2020 Status Report).

¹⁵ As at January, 2021.

¹⁶ BlackRock, Larry Fink’s 2021 Letter to CEOs (January 2021) <<https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter>>.

¹⁷ *Ibid.*

¹⁸ For audit committee guidance, see Janis Sarra, Canada Climate Law Initiative, *Audit Committees and Effective Climate Governance, A Guide for Boards of Directors* (December 2020) <<https://ccli.ubc.ca/wp-content/uploads/2021/04/Guide-for-Audit-Committees-on-Effective-Climate-Governance.pdf>> and *A Closer Look*, a Primer for audit committee members produced by Deloitte UK for Chapter Zero, the CGI’s UK Chapter and made available to the global network of Chapters. The Primer is also available in Spanish through the CGI’s Latin American Chapters.

¹⁹ Sarah Barker, Alexia Staker and Alice Garton, Commonwealth Climate and Law Initiative (CCLI), *Concerns Misplaced: Will compliance with the TCFD recommendations really expose companies and directors to liability risk?* (September 2017), 9 <<https://ccli.ouce.ox.ac.uk/wp-content/uploads/2017/10/CCLI-TCFD-Concerns-Misplaced-Report-Final-Briefing.pdf>>.

In short, disclosure of forward-looking risks associated with climate change – with adequate specificity and relevance, and with appropriate cautionary language around associated limitations or uncertainties – is the best (if not only) way to minimise liability exposure for misleading disclosure. Whilst appropriate analysis and disclosure will be company-specific, the TCFD recommendations represent an influential touchstone for the processes required to robustly assess climate risks (and opportunities), and to communicate them to the market in a true and fair manner.²⁰

²⁰ *Ibid.*, 13.



4. Litigation

4. Litigation

Data on climate litigation to date show that as of the end of 2020, at least 1,550 cases involving climate change had been brought globally, in 38 countries.²¹ While only a few of these cases to date involve fiduciary duty or securities claims, this is likely to change as this field of litigation expands. Those fiduciary duty and securities claims that have been brought clearly show the risks to companies, and their directors and officers, from failing to incorporate climate change into strategy, oversight, risk management and disclosure.

For instance, in 2018, a successful claim was brought against Polish power generation company Enea SA seeking the annulment of a board resolution consenting to the construction of the €1.2bn 1GW Ostrołęka C coal-fired power plant, on the basis that construction would harm the economic interests of the company by failing to consider the transition risks posed by climate change.²² In Australia, the corporate trustee of A\$50 billion AUM pension fund REST was sued for breach of its duty of care for failing to integrate climate change considerations into its investment strategy.²³ The case was settled in November 2020 on favourable terms to the plaintiff. REST issued a press release recognizing climate change as a material financial risk, and undertook to be net-zero by 2050 and to ensure that its investment managers “take active steps to consider, measure, and manage financial risks posed by climate change and other relevant ESG risks.”²⁴ In the U.S., ExxonMobil and its officers have been sued for breach of fiduciary duty and securities fraud. The earliest of these claims, *Ramirez v ExxonMobil*, passed a key hurdle in 2018 when Judge Kinkeade for the Northern District of Texas allowed the case regarding the company’s liability and that of individual officers and directors to go forward.²⁵ The court held that the plaintiffs’ allegations supported a strong inference that the defendants had actual awareness or knowledge that ExxonMobil had materially misrepresented the value of its assets (which the plaintiffs alleged the company and its individual officers Tillerson, Swiger, and Rosenthal knew would need to be written down as oil prices started to collapse in 2014,

²¹ UNEP and Sabin Center for Climate Change Law, *Global Climate Litigation Report: 2020 Status Review* (2020)

<<https://wedocs.unep.org/bitstream/handle/20.500.11822/34818/GCLR.pdf?sequence=1&isAllowed=y>> (stating that as of the end of 2020, there were 1550 climate change cases in 38 countries, of which 1,200 were filed in the U.S. against federal, state, municipal governments, fossil fuel companies, coal companies, and electrical companies and their officers and directors).

²² *ClientEarth v Enea*, District Court of Poznań [31 July 2019] <http://climatecasechart.com/non-us-case/clientearth-v-enea/>>. The Court found in ClientEarth’s favour on the first ground (the board resolution approving the power plant was legally invalid under Polish company law) so the judge did not need to formally determine the second ground (climate risk).

²³ *McVeigh v REST* NSD1333/2018, Federal Court of Australia, <<http://climatecasechart.com/non-us-case/mcveigh-v-retail-employees-superannuation-trust/>>.

²⁴ See *Statement of REST*, available at <<https://equitygenerationlawyers.com/cases/mcveigh-v-rest/>>. The pleadings are available at <<http://climatecasechart.com/non-us-case/mcveigh-v-retail-employees-superannuation-trust/>>.

²⁵ *Ramirez v Exxon Mobil*, 334 F.Supp.3d 832, 839-841 (N.D.Tex.2018) (Memorandum Opinion and Order).

and as oil sands investments looked increasingly likely to become “stranded assets.”)²⁶ That litigation is ongoing.

Litigation and liability risks are real, both for directors personally and for the company. The most recent indication of this point was the decision by the District Court in The Hague ordering Royal Dutch Shell to cut its CO₂ emissions by 45% by the end of 2030, compared to 2019 levels.²⁷ That decision is being appealed, but it is stark evidence of a shift in the zeitgeist concerning companies' climate responsibilities, and Royal Dutch Shell has meanwhile indicated it will initiate efforts to comply. Governance mechanisms to mitigate the risks of climate litigation and even potentially personal liability ought therefore to be prioritized by forward-thinking boards.²⁸ This Primer is being published in order to help guide thinking about those governance mechanisms.

²⁶ *Ibid.*

²⁷ The decision in English is available at: *Milieudefensie et al. v. Royal Dutch Shell PLC* C/09/571932 / HA ZA 19-379 (engelse versie), <<https://uitspraken.rechtspraak.nl/inziendocument?id=ECLI:NL:RBDHA:2021:5339>>.

²⁸ Comprehensive databases discussing climate litigation to date are available from the Sabin Centre at Columbia University, Climate Change Litigation Database, <<http://climatecasechart.com/>>, and from the Grantham Centre at the London School of Economics, <<https://climate-laws.org/>>.



5. Questions to Assist Directors

5. Questions to Assist Directors

The actions required to fulfil directors' duties and disclosure obligations will depend on the laws of the jurisdiction and unique circumstances of the company and situation.

To assist directors, we offer some high-level questions:

- Does my board actively consider the foreseeable and material financial risks to the company associated with climate change and the potential impacts on corporate risk management and strategy?
- Do I meaningfully engage with and scrutinise information and advice concerning climate-related risks presented to the board? Do I need to seek independent advice?
- If climate change is never on the board agenda or in management reports, do I ask why not?
- Does my board consider climate risks, both in relation to general strategic planning and risk management, and in relation to specific projects or acquisitions that require board oversight or approval?
- Has my company embedded robust procedures to ensure that foreseeable and financially material climate risks are identified, dynamically managed, and appropriately reported to the board and in the financial statements and external reporting?
- Do I have a sufficient level of knowledge on the physical, transition, liability, and systemic risks associated with climate change to fulfil my duties to govern the management of these risks? Does my board identify potential knowledge gaps among board members and organise appropriate training, and/or commission independent expert advice, to address them?

In each country section, experts offer their views about corporate governance mechanisms and approaches boards should adopt to ameliorate climate change risks, and to better identify opportunities.



5. Jurisdictional Overviews

6. Jurisdictional Overviews

This section summarises the law on directors' duties and disclosure obligations in respect of climate change across some important commercial jurisdictions around the world. In a growing number of jurisdictions, published legal opinions and regulatory guidance have clarified that financially material climate-related risks can and should be integrated into board strategy and risk management practices in order to fulfil directors' duties and form an increasingly central part of their disclosure responsibilities.

To read a specific jurisdictional overview, please click on the name of the country or jurisdiction on the map.



Australia

In Australia, regulator statements acknowledge the foreseeability of climate-related financial risks. The Reserve Bank of Australia's (RBA) Deputy Governor described the physical and transition risks associated with climate change as "likely to have first-order economic effects".²⁹ The RBA's 2019 half-yearly Financial Stability Review devoted a section to climate change.³⁰ The Australian Securities and Investments Commission (ASIC) has similarly characterised climate change as a "systemic risk that could have a material impact on the future financial position, performance or prospects of entities".³¹ The Council of Financial Regulators has established a working group on the financial implications of climate change to help coordinate agencies' actions.³² The Australian Prudential Regulation Authority (APRA) has emphasised that climate risks should be managed like any other risk, in line with existing prudential risk management standards,³³ as well as the new Prudential Practice Guide CPG 229 Climate Change Financial Risks (CPG 229). APRA is increasing its scrutiny of institutions' climate risk management and will factor this into its ongoing supervisory activities and stress tests.³⁴

In short, the position in Australia is clear: climate change is a financial risk that must be addressed by directors through governance and disclosure practices.

Directors' Duties and Climate Change

Australia is a common law jurisdiction. In Australia, directors' common law and equitable duties have been codified in the *Corporations Act 2001* (Cth).³⁵ However, the general law duties continue to apply concurrently.³⁶ Directors must exercise their powers and discharge their duties in "good

²⁹ Guy Debelle, 'Climate Change and the Economy,' Speech at the Public Forum hosted by the Centre for Policy Development, Sydney (March 2019) <<https://www.rba.gov.au/speeches/2019/sp-dg-2019-03-12.html>>.

³⁰ Reserve Bank of Australia, *Financial Stability Review* (October 2019) <<https://www.rba.gov.au/publications/fsr/2019/oct/box-c-financial-stability-risks-from-climate-change.html>>.

³¹ ASIC, 'RG 247 Effective disclosure in an operating and financial review' (August 2019) <<https://download.asic.gov.au/media/5230063/rg247-published-12-august-2019.pdf>>.

³² Reserve Bank of Australia, *Financial Stability Review* (October 2018) <<https://www.rba.gov.au/publications/fsr/2018/oct/regulatory-developments.html>>.

³³ Summerhayes G, 'Australia's new horizon: Climate change challenges and prudential risk', Speech at the Insurance Council of Australia Annual Forum, Sydney (17 February 2017) and Summerhayes G, 'Financial exposure: the role of disclosure in addressing the climate data deficit', Speech at ClimateWise and University of Cambridge Institute for Sustainable Leadership, London, (22 February 2019); APRA, 'APRA releases guidance on managing the financial risks of climate change' (22 April 2021) APRA Website <<https://www.apra.gov.au/news-and-publications/apra-releases-guidance-on-managing-financial-risks-of-climate-change>>.

³⁴ APRA, 'Information Paper: APRA's Supervision Priorities' (February 2021) APRA Website <<https://www.apra.gov.au/sites/default/files/2021-01/Information%20Paper%20-%20Supervision%20Priorities%202021.pdf>>.

³⁵ *Corporations Act 2001* (Cth) sections 180-183.

³⁶ *ibid* section 185.

faith in the best interests of the corporation”, and for a “proper purpose”. The general duty of due care and diligence requires directors to “exercise their powers and discharge their duties with the degree of due care and diligence that a reasonable person would exercise” in the relevant circumstances.

In October 2016, Australian barrister Noel Hutley SC released a seminal legal opinion on directors' statutory duty of care as it applies to climate change (the [Hutley opinion](#)). Hutley SC concluded that, as a matter of Australian law, “climate change risks would be regarded as foreseeable by courts, and relevant to a director's duty of care to the extent that those risks intersect with the interests of the company”. Accordingly, Australian company directors certainly can, and in some cases *should* be considering the impact of climate change risks on their company – and those directors who fail to do so now could conceivably be found liable for breaching their duty of care in the future.³⁷

In June 2018, ASIC Commissioner John Price made public remarks foreshadowing that directorial liability could arise from a failure to consider risks related to climate change.³⁸ In September 2018, ASIC recommended that:

directors and senior managers of listed companies need to understand and continually reassess existing and emerging risks that may be applicable to the company's business, including climate risk.³⁹

In March 2019, Hutley SC updated his 2016 legal opinion, concluding that there had been a demonstrable shift since 2016 in the way in which Australian regulators, firms and the public perceive climate risk which “elevate[d] the standard of care that will be expected of a reasonable director” in discharging their duty of care.⁴⁰

In November 2019, former Australian High Court judge and financial services royal commissioner Kenneth Hayne stated that it is incumbent on company directors, in discharging their duty to act in the company's best interests, to consider, address and report on climate-related risks:

³⁷ Noel Hutley SC and Sebastian Hartford-Davis, 'Climate Change and Directors' Duties: Memorandum of Opinion' (October 2016), 2-3 <<https://cpd.org.au/wp-content/uploads/2016/10/Legal-Opinion-on-Climate-Change-and-Directors-Duties.pdf>>.

³⁸ John Price, 'Climate Change', Speech at the Australian Securities and Investments Commission, Centre for Policy Development: Financing a Sustainable Economy, Sydney, (18 June 2018) <<https://asic.gov.au/about-asic/news-centre/speeches/climate-change/>>. ASIC Commissioners Sean Hughes (Canberra, 7 February 2019) and Cathie Armour (Sydney, 21 February 2019) also made public addresses concerning climate change risk.

³⁹ ASIC, 'Report 593: Climate risk disclosure by Australia's listed companies' (September 2018), 12 <<https://download.asic.gov.au/media/4871341/rep593-published-20-september-2018.pdf>>.

⁴⁰ Noel Hutley SC and Sebastian Hartford-Davis, 'Climate Change and Directors' Duties: Supplementary memorandum of opinion' (March 2019) <<https://cpd.org.au/2019/03/directors-duties-2019/>>.

[A] director acting in the best interests of the company must take account of, and the board must report publicly on, climate-related risks and issues relevant to the entity.⁴¹

In April 2021, Hutley SC published a further update to the 2016 legal opinion, stating that:

[i]t is no longer safe to assume that directors adequately discharge their duties simply by considering and disclosing climate-related trends and risks; in relevant sectors, directors of listed companies must also take reasonable steps to see that positive action is taken: to identify and manage risks, to design and implement strategies, to select and use appropriate standards, to make accurate assessments and disclosures, and to deliver on their company's public commitments and targets.⁴²

Counsel further opined that in relevant sectors, consideration of net zero emissions targets are an "appropriate and necessary" step to discharge duties. In setting such targets, a company need not have all the answers about how the target will be achieved. However, an announcement of a net zero target carries with it a representation that a company does have a genuine intention, formed on reasonable grounds at the time of making the commitment, to pursue strategies to achieve the target in good faith. Misalignment between that intention and operational strategy places the company, and its directors and officers, at risk of 'greenwash', and potentially liable for misleading and deceptive conduct in relation to a 'future matter' under the *Corporations Act, Australian Securities and Investments Commission Act 2001*, and the Australian Consumer Law. This may, in turn, lead to 'stepping stone' liability for a breach of the directors' duty of care. Indeed, Counsel was of the view that "there is reason to think that 'greenwashing' claims of the kind outlined in this memorandum will become an acute source of risk".⁴³

⁴¹ Kenneth Hayne, 'What Kenneth Hayne says about climate change' (9 December 2019) <<https://www.afr.com/politics/federal/what-kenneth-hayne-says-about-climate-change-20191206-p53hiw>>; James Fernyhough, 'Hayne rebukes directors on climate risk failure' (9 December 2019) <<https://www.afr.com/policy/energy-and-climate/hayne-rebukes-directors-on-climate-risk-failure-20191206-p53hnd>>; Ben Hayne, 'No more room for excuses on climate' (9 December 2019) <<https://www.afr.com/politics/federal/no-more-room-for-excuses-on-climate-20191208-p53hkw>>. Centre for Policy development, 'Full text of Kenneth Hayne AC QC remarks to CPD climate roundtable', Speech delivered to Centre for Policy Development Roundtable in Sydney, 21 November 2019 (9 December 2019) <<https://cpd.org.au/2019/12/full-text-of-kenneth-hayne-ac-qc-remarks-to-cpd-climate-roundtable/>>.

⁴² Noel Hutley and Sebastian Hartford Davis, 'Climate Change and Directors' Duties: Further Supplementary Memorandum of Opinion' (23 April 2021) [4] <<https://cpd.org.au/wp-content/uploads/2021/04/Further-Supplementary-Opinion-2021-3.pdf>>. See further, MinterEllison, 'New Hutley Opinion: What does it mean for directors?', (28 April 2021) <<https://www.minterellison.com/articles/new-hutley-opinion-what-does-it-mean-for-directors>>.

⁴³ Noel Hutley and Sebastian Hartford Davis, 'Climate Change and Directors' Duties: Further Supplementary Memorandum of Opinion' (23 April 2021) [50] <<https://cpd.org.au/wp-content/uploads/2021/04/Further-Supplementary-Opinion-2021-3.pdf>>.

Directors' Disclosure Obligations and Climate Change

The securities regulator ASIC has recommended that listed companies disclose meaningful and useful climate risk-related information to investors, and strongly encouraged listed companies with material exposure to climate change to consider reporting voluntarily under the TCFD framework.⁴⁴ The Australian Securities Exchange (ASX) Corporate Governance Council recommends that a listed entity should disclose (on a comply or explain basis) whether it has any material exposure to environmental risks and, in particular, climate-related risk, and if it does, how it manages or intends to manage those risks.⁴⁵

In August 2019, ASIC revised its regulatory guidance to incorporate climate-related disclosures. RG228 now refers to the types of climate change risk described by the TCFD as key risks that may need to be disclosed in prospectuses.⁴⁶ RG47 highlights climate change as a “systemic risk” that could impact an entity’s financial prospects for future years and that may need to be disclosed in operating & financial reviews.⁴⁷

In April 2019, the Australian Accounting Standards Board and Auditing and Assurance Standards Board updated their joint bulletin on integrating climate risk into accounting estimate assumptions and making climate risk disclosures in the financial statements, squarely bringing climate risk within the scope of external audit and the audit committee role.⁴⁸ These developments are relevant to the obligation on Australian directors to give a declaration that the financial statements and notes comply with the accounting standards and give a 'true and fair view' of position and performance.⁴⁹

Practical Implications for Directors

The steps required to discharge duties to govern and disclose climate risk depend on the unique circumstances of the company and governance situation. However, given that Australia’s financial regulators have become increasingly emphatic regarding the need for companies and their directors

⁴⁴ ASIC, 'Report 593: Climate risk disclosure by Australia's listed companies' (September 2018) 12 <<https://download.asic.gov.au/media/4871341/rep593-published-20-september-2018.pdf>>

⁴⁵ The ASX Corporate Governance Council 'Corporate Governance Principles and Recommendations' (4th Edition, February 2019) 27-28.

⁴⁶ ASIC, Regulatory Guide G228 *Prospectuses: Effective disclosure for retail investors* <<https://asic.gov.au/regulatory-resources/find-a-document/regulatory-guides/rq-228-prospectuses-effective-disclosure-for-retail-investors/>>.

⁴⁷ ASIC, Regulatory Guide 247 *Effective disclosure in an operating and financial review* (August 2019) <<https://asic.gov.au/regulatory-resources/find-a-document/regulatory-guides/rq-247-effective-disclosure-in-an-operating-and-financial-review/>>.

⁴⁸ Australian Accounting Standards Board and Australian Auditing and Assurance Standards Board, 'Climate-related and other emerging risks disclosures: assessing financial statement materiality using AASB/IASB Practice Statement 2' (April 2019) <https://www.aasb.gov.au/admin/file/content102/c3/AASB_AUASB_Joint_Bulletin_Finished.pdf>.

⁴⁹ *Corporations Act 2001* (Cth) sections 295-297.

to adopt climate risk and resilience measures in business practices and disclosure, and in particular the above-noted Hutley opinions, actions by ASIC and the Australian Accounting Standards Board and Auditing and Assurance Standards Board, well-counselled boards will, taking into account the unique circumstances facing each company:⁵⁰

- a) maintain systems so that the board and management have the skills and education to remain abreast of material developments in this dynamic area, including access to expert advice where necessary and when not available internally;
- b) delegate climate risk identification and evaluation to a clearly-identified team in management that reports directly to the CEO and board;
- c) put on the agenda for the board, within a reasonable time, a process to start developing a climate transition roadmap to 2050 with transparent net zero emissions targets (for relevant sectors) or other robust emissions reduction targets, with clear interim targets, and periodically thereafter report back to the board;
- d) where board sub-committees are used, delegate to the appropriate committee(s) of the board, such as risk, audit, legal and governance, scenarios/strategy, nominations/remuneration, or sustainability/corporate responsibility, the task of translating the long-term strategy into a clear decision-making process for each aspect that is relevant to each committee; and
- e) examine reporting and disclosure frameworks and guidance so that disclosures are meeting regulatory (and where relevant investor) expectations and oversee a communication and engagement plan so that there is accountability to stakeholders.

Contributors: Sarah Barker, MinterEllison
Ellie Mulholland, CCLI, MinterEllison
CCLI

MinterEllison



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Climate and Law Initiative

Australian
Institute of
Company
Directors

⁵⁰ These include size and sector, the foreseeability and materiality of exposure to climate risks, and that the steps required to discharge duties will be proportionate to that exposure.

Brazil

Brazil is a signatory to the United Nations Framework Convention on Climate Change International Climate Change Agreement (Paris Agreement), which was transformed into a federal law by means of Federal Decree No.9.073/2017. In December 2019, the Environmental Committee of the Federal Senate conducted an evaluation of the National Policy on Climate Change, to assess the main difficulties facing its enforcement and to identify the areas requiring amendment. This assessment resulted, among others, in Constitutional Amendment Bill No.233/2019, which aims to include in the Brazilian Federal Constitution a provision stating that all economic activity in Brazil must be guided by the need to “promote climate stability, by usage of mitigating measures to prevent climate change and adapt to its negative effects”.

Directors' Duties and Climate Change

Limited liability companies (*sociedades limitadas*) and corporations (*sociedades anônimas*) are the most common types of companies in Brazil and are legally formed as for-profit organizations. The Brazilian legal framework, in particular (i) the *Federal Constitution of 1988*, as amended (Brazilian Federal Constitution), (ii) *Law No.10.406, as of 10 January 2002*, as amended (Brazilian Civil Code⁵¹), and (iii) *Law No.6.404, as of 15 December 1976*, as amended (Brazilian Corporation Law), provide, at least indirectly, that companies must follow sustainability and climate-related principles alongside their corporate purpose.

The Brazilian legal system lays out a series of principles that guide the conduct of economic activity, such as the social function of ownership, the social function of contracts, environmental protection, and the reduction of regional and social inequities, as stated in the Brazilian Federal Constitution⁵² and in the Brazilian Civil Code.⁵³ Generally speaking, these principles apply to all entities comprising the Brazilian economy and, thus, it could be argued that all corporations and limited liability companies, including their directors and administrators, have an implicit duty to employ

⁵¹ Available in English at http://conteudo.cvm.gov.br/export/sites/cvm/subportal_ingles/menu/investors/anexos/Law-6.404-ing.pdf Retrieved on November 17, 2020.

⁵² Article 170 of the Brazilian Federal Constitution. “The economic order, founded on the appreciation of the value of human work and on free enterprise, is intended to ensure everyone a life with dignity, in accordance with the dictates of social justice, with due regard for the following principles: [...] III – the social function of ownership; [...] VI – environment protection, which may include differentiated treatment in accordance with the environmental impact of goods and services and of their respective production and delivery processes; [...] VII – reduction of regional and social differences; [...]”.

⁵³ Article 421 of the Brazilian Civil Code. “The contractual freedom shall be exercised within the limits of the social function of the contract.”

best efforts to, at least, minimize negative sustainability impacts, including climate change.

Moreover, Brazilian Corporation Law also focuses indirectly on sustainability matters, assigning fiduciary responsibility to managers and controlling shareholders. In this regard, articles 116⁵⁴ and 154⁵⁵ of the Brazilian Corporation Law contain provisions regarding the need to harmonize the interest of each company in generating profits with its socio-environmental impacts.⁵⁶ In this sense, Item VI of article 170 of the Brazilian Federal Constitution also states that all economic or financial activity conducted in Brazil must be guided by the principle of environmental protection.⁵⁷

Additionally, Brazilian Environmental Policy imposes a series of procedures to prevent, mitigate and repair environmental damage, which must be observed by all companies. Although there are no specific duties for directors on climate change, if companies fail to observe these norms and contribute – even indirectly – to environmental damage, they may be liable in civil court for strict, joint and several liability for environmental degradation.

Furthermore, *Law No.9.605, of 12 February 1998*, which establishes the Brazilian environmental crimes and administrative sanctions, imposes criminal and administrative penalties on individuals and legal entities whose conduct and activities are damaging to the environment. Individuals (such as directors)⁵⁸ or legal entities that commit a criminal offence against the environment may also be punished with sanctions that range from fines to

⁵⁴ A controlling shareholder shall use its controlling power in order to make the corporation accomplish its purpose and perform its social role, and shall have duties and responsibilities towards the other shareholders of the corporation, those who work for the corporation and the community in which it operates, the rights and interests of which the controlling shareholder must loyally respect and heed.

⁵⁵ An officer shall use the powers conferred upon him by law and by the bylaws to achieve the corporation's corporate purposes and to support its best interests, including the requirements of the public at large and of the social role of the corporation.

⁵⁶ Article 154, paragraph 4 of the Brazilian Corporation Law. In view of the corporation's social responsibilities, the administrative council or the board of directors may authorize the performance of reasonable gratuitous acts to benefit the employees or the community to which the corporation belongs.

⁵⁷ On this subject, the Brazilian Federal Supreme Court rendered a decision stating that "economic activity must not be enacted in opposition to the principles established to enforce environmental protection." (Brazilian Federal Supreme Court, Direct Action for the Declaration of Unconstitutionality No.3,540, Judge Rapporteur Justice Celso de Mello, judgement rendered on 09.01.2005, published on 2 March 2006). Pursuant to Article 927 of the Brazilian Code of Civil Procedure (*Federal Law No. 13,105, of 16 March 2015*), this a binding precedent that must be observed by the courts.

⁵⁸ It is important to mention that in the case of the Samarco's dam collapse, board directors of Vale and BHP were included as defendants in a criminal proceeding regarding the accident. However, according to public information, the action was dismissed in respect of some of these directors because the judge considered that they did not have the power to influence the company's management, so could not be regarded as having committed the crimes themselves. Furthermore, there is also an administrative proceeding before the Brazilian Securities Commission (CMV) to investigate any violation of the fiduciary duty of some of the board directors of Vale due to the Brumadinho dam collapse. There is no public information available regarding this proceeding.

imprisonment (individuals) or dissolution (legal entities). Administrative liability further includes the imposition of fines and, in worst-case scenarios, the total suspension of activities. It is important to note that, pursuant to *Law No.9.605*, shareholders may be held liable through the piercing of the corporate veil, which will be admitted whenever the corporate entity becomes an obstacle to the recovery of environmental damages.

Therefore, despite the fact that most current laws and regulations do not directly require directors to consider climate change matters, when analysing the Brazilian legal framework, it is possible to argue that board directors and controlling shareholders, could, in some cases, potentially be in breach of their fiduciary duties in the event that they pursue goals that, in any manner, are contrary to the long-term interests of their community and society as a whole and, to this end, contrary to preventing climate change.

Besides legislation and regulations, sustainability-related matters have gained increasing prominence in the Brazilian financial and capital markets, as several Brazilian stakeholders have recently been taking initiatives or shown their concern for sustainability and environmental impact. For instance, the Social and Economic Development Bank (*Banco Nacional do Desenvolvimento Econômico e Social – BNDES*) has recently included the generation of positive sustainability impact in the qualification requirements of its tendering processes, and has also adopted a screening process to filter projects with negative sustainability impact out of its portfolio. In addition, the Central Bank of Brazil recently released its sustainability agenda for the coming years, which expressly includes (i) incorporation of climate risk scenarios into new and improved stress tests of the bank and (ii) increasing transparency based on TCFD recommendations.

Director's Disclosure Obligations and Climate Change

Brazilian Corporation Law charges the board directors and other bodies comprising limited liability companies and corporations with the duty to disclose, in general and whenever necessary, all information that may negatively affect the environment, among others. The duty to inform, in addition to best practices as defined by Brazilian soft law, create the conditions for investors, the market and supervisory bodies to conduct complex analyses of the actions taken by companies and their impacts on the environment and other sustainability issues.

In this regard, Rule No.480/09 of the Securities and Exchange Commission of Brazil (*Comissão de Valores Mobiliários – CVM*) establishes an obligation for publicly-held corporations to disclose in their filings (i) risk factors related to environmental matters, (ii) the effects of regulation on the company's environmental policy and compliance costs and (iii) information related to the company's environmental policy. Thus, although currently there are no specific provisions on the obligation to provide information on climate

change, directors should be aware of how their decisions impact the information the company discloses on this subject within the required section on broader environmental risk factors. Furthermore, it is important to state that Rule No.480/09 is under revision, and one of the proposed alterations is to expressly include a risk factor regarding climate change.

The Corporate Sustainability Index (*Índice de Sustentabilidade Empresarial* - ISE B3), a voluntary initiative that classifies publicly-held corporations with regard to sustainability matters, also sets out a series of details that must be presented by the selected companies in relation to the environment, with a specific questionnaire on climate change. Among other information, companies are required to disclose an assessment of both their impact on the climate and their exposure to climate-related impacts, as well as their plans to manage and prevent such impacts.

Another voluntary initiative is the CDP Brazil Climate Resilience Index, created in March 2020 by the British NGO Carbon Disclosure Project (CDP). This index aims to establish a connection between companies' disclosure of environmental data and their financial performance. It serves as a reference for investors to assess the companies' transparency regarding the policies and actions adopted in relation to climate change, reinforcing the drivers seen in Brazilian capital markets for directors to take responsibility for their decisions regarding climate-related disclosures.

Practical Implications for Directors

Given that Brazilian representatives and regulators have become increasingly emphatic in recommending – and soon regulating – the need for companies and their directors to adopt climate resilience measures in business practices and disclosure, in particular the above-noted *Constitutional Amendment Bill No.233/2019*, the Brazilian Civil Code, Brazilian Corporation Law, Brazilian Environmental Policy and the CVM's Rule No.480/09, together with related public and private financial institutions initiatives, well-counselled boards will:

- a) delegate climate risk identification and evaluation to a clearly-identified team in management which reports directly to the CEO and board;
- b) put on the agenda for the board within 3 or 6 months a process to initiate the development of a climate transition roadmap to 2050 with transparent carbon neutrality or reduction targets, with clear interim targets to 2040, 2030 and the current rolling multi-year strategic plan, and periodically thereafter report back to the board;
- c) delegate to the appropriate committee(s) of the board, such as risk, audit, legal and governance, scenarios/strategy,

nominations/remuneration, or sustainability/corporate responsibility, the task of translating the long-term strategy into a clear decision-making process for each aspect that is relevant to each committee; and

- d) discuss with disclosure counsel, in order to develop an external engagement and communications plan.

Contributors: Lina Pimentel Garcia, Mattos Filho Brazil

Tábata Boccanera Guerra de Oliveira, Mattos Filho Brazil



Canada

In Canada, the Pan-Canadian Framework on Clean Growth and Climate Change has been agreed by the federal government and most of the provinces and territories as of December 2016.⁵⁹ That Framework established a goal of reducing Canada's greenhouse gas emissions by 30% below 2005 levels by 2030 to meet Canada's commitments to the Paris Agreement. In April 2021, the Government increased its ambition, pledging 40 to 45% reductions by 2030, enhancing its 2020 commitment of achieving net-zero emissions by 2050.⁶⁰ The Pan-Canadian Framework established a price on carbon as its central policy tool, and subsequent legislation enacted a backstop price on carbon if individual provinces refused to put a price in place. Canada's *Greenhouse Gas Pollution Pricing Act* was found to be constitutionally valid by the Supreme Court of Canada in April of 2021.⁶¹

Federal regulators have also acknowledged the risks to the Canadian economy if Canada fails to address climate change. In 2019, in its Annual Financial System Review, the Bank of Canada for the first time discussed climate change as a vulnerability to both Canada's economy and its financial system.⁶² In November 2020, the Bank of Canada and the Office of the Superintendent of Financial Institutions (OSFI) launched a pilot project to use climate change scenarios to better understand the risks to the financial system related to a transition to a low-carbon economy.⁶³ The OSFI also published a study in 2021 recognizing that climate-related transition risks can lead to reduced profitability, stranded assets, inability to make loan repayments and/or attract investments, and loss of market capitalization.⁶⁴ The federal government's 2021 budget announced that Canada's Crown corporations will demonstrate climate leadership by adopting the Task Force on Climate-related Financial Disclosures standards or more rigorous standards as part of their corporate reporting, mandatory for corporations with over CAD\$1 billion in assets. Crown corporations with less than CAD\$1 billion in assets will be expected to start reporting on their climate-related

⁵⁹ Government of Canada, Pan-Canadian Framework on Clean Growth and Climate Change (2016) <<https://www.canada.ca/en/services/environment/weather/climatechange/pan-canadian-framework.html>>.

⁶⁰ Prime Minister Trudeau, Government of Canada statement, (22 April 2021), <<https://pm.gc.ca/en/news/news-releases/2021/04/22/prime-minister-trudeau-announces-increased-climate-ambition>>; Government of Canada, *Net Zero by 2050*, <<https://www.canada.ca/en/services/environment/weather/climatechange/climate-plan/net-zero-emissions-2050.html>>.

⁶¹ Reference re *Greenhouse Gas Pollution Pricing Act*, 2021 SCC 11 at [2].

⁶² Bank of Canada, *Financial System Review 2020*, Vulnerability 5, Climate Change, (14 May 2020) <<https://www.bankofcanada.ca/2019/05/financial-system-review-2019/#Vulnerability-5-Climate-change>>.

⁶³ Bank of Canada, Press Release, *Bank of Canada and OSFI launch pilot project on climate risk scenarios*, (16 November 2020) <<https://www.bankofcanada.ca/2020/11/bank-canada-osfi-launch-pilot-project-climate-risk-scenarios/>>.

⁶⁴ OSFI, 'Navigating Uncertainty in Climate Change, Promoting Preparedness and Resilience to Climate-related Risks', (January 2021), 9 <<https://www.osfi-bsif.gc.ca/Eng/Docs/clmt-rsk.pdf>>.

financial risks by 2024 or provide justification as to why climate risks do not have material impact on their operations.⁶⁵

Directors' Duties and Climate Change

The *Canada Business Corporations Act* and its sister corporation statutes in the provinces and territories codify and enhance directors' common law duties of loyalty and care. The corporate statutory duty of loyalty requires the directors and officers of a corporation to "act honestly and in good faith with a view to the best interests of the corporation".⁶⁶ The Supreme Court of Canada has held that the duty of care requires the directors and officers to "exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances".⁶⁷ The court will defer to the reasonable business judgment of directors who have been duly diligent in their oversight of the company.⁶⁸ In June 2020, corporate lawyer and board governance expert Carol Hansell from law firm Hansell LPP issued a legal opinion on directors' obligations to address climate change under Canadian law (the [Hansell opinion](#)).⁶⁹ The legal opinion identifies both directors' fiduciary duty of loyalty⁷⁰ and their duty of care⁷¹ as requiring engagement and consideration of climate-related risk. In order to discharge their duty to act in the best interests of the company, directors must consider the long-term interests of the company and, to this end, any environmental risks.⁷² Directors' duty of care requires that they solicit reports and recommendations from management and external sources on climate-related risk as necessary and be satisfied that the company is addressing climate change risk appropriately.⁷³

⁶⁵ Government of Canada, 2021 Federal Budget, a recovery plan for Jobs, Growth and Resilience (2021), 175-176 <<https://www.budget.gc.ca/2021/home-accueil-en.html>>.

⁶⁶ *Canada Business Corporations Act*, note 24, section 122(1) and its sister provincial and territorial corporations statutes.

⁶⁷ *Peoples Department Stores Inc (Trustee of) v Wise*, 2004 SCC 68, [2004] 3 SCR 461; *BCE Inc v 1976 Debentureholders*, 2008 SCC 69 at [39], [2008] 3 SCR 560; Janis Sarra, *Canada Climate Law Initiative Fiduciary Obligations in Business and Investment: Implications of Climate Change* (April 2018) <<https://ccli.ubc.ca/wp-content/uploads/2021/04/Fiduciary-Obligation-in-Business-and-Investment.pdf>>.

⁶⁸ *Ibid.*

⁶⁹ Hansell LLP, 'Legal Opinion: Putting Climate Change Risk on the Boardroom Table' (June 2020) <<https://www.hanselladvisory.com/content/uploads/Hansell-Climate-Change-Opinion.pdf>>.

⁷⁰ CBCA, s 122(1)(a)

⁷¹ *Peoples Department Stores Inc (Trustee of) v Wise*, 2004 SCC 68, [2004] 3 SCR 461.

⁷² Hansell LLP, 'Legal Opinion: Putting Climate Change Risk on the Boardroom Table' (June 2020), 16-17 <<https://www.hanselladvisory.com/content/uploads/Hansell-Climate-Change-Opinion.pdf>>.

⁷³ Hansell LLP, 'Legal Opinion: Putting Climate Change Risk on the Boardroom Table' (June 2020), 13-15 <<https://www.hanselladvisory.com/content/uploads/Hansell-Climate-Change-Opinion.pdf>>.

See also Janis Sarra, *Duty to Protect: Corporate Directors and Climate-Related Financial Risk* (January 2021) <<https://ccli.ubc.ca/wp-content/uploads/2021/04/Duty-to-Protect-Corporate-Directors-and-Climate-Related-Financial-Risk.pdf>>.

Directors' Disclosure Obligations and Climate Change

Canadian securities regulators have advised that climate change risk is now widely recognised as a mainstream business issue and that companies must disclose material climate risks and how they are addressing them.⁷⁴ A Canadian Securities Administrators (CSA) report states that despite the potential uncertainties and longer time horizon associated with climate change-related risks, boards and management should take appropriate steps to understand and assess the materiality of these risks to their business.⁷⁵

The CSA has given notice that the board and management should assess their expertise with respect to sector-specific climate-related risks, and augment that expertise, as necessary.⁷⁶ CSA Staff Notice 51-358 Reporting of Climate Change-related Risks states that the audit committee and the board should be provided with appropriate orientation and information to help members understand sector-specific climate-related issues.⁷⁷ It suggests that the board ask itself whether directors have been provided sufficient information, including management's materiality assessments in respect of the issuer's climate-related risks, to appropriately oversee and consider management's assessment of these risks.⁷⁸ CSA Staff Notice 51-358 states:

An assessment of materiality in relation to climate change-related risks may require issuers to adapt their existing approaches to risk assessments in order to better understand the potential impacts of climate change-related risks and their materiality. In some cases, this may involve adjusting their approaches to consider the longer time horizon associated with and how to effectively quantify these types of risks.⁷⁹

The Hansell opinion concluded that public companies' disclosure obligations under securities law extend to the disclosure of climate-related risks (and opportunities).⁸⁰ Hansell reported that "Directors should also be aware that their decisions about disclosure are not protected by the business judgment rule."⁸¹

The Canadian government in its 2019 budget endorsed the TCFD's international disclosure standards and called for a phased approach to

⁷⁴ CSA Staff Notice 51-358 *Reporting of Climate Change-related Risks* (2019), <https://www.osc.gov.on.ca/en/SecuritiesLaw_csa_20190801_51-358_reporting-of-climate-change-related-risks.htm>. See also CSA Staff Notice 51-333 Environmental Reporting Guidance (SN 51-333).

⁷⁵ CSA Staff Notice 51-358, *ibid* at 4.

⁷⁶ *Ibid*.

⁷⁷ *Ibid*.

⁷⁸ *Ibid*.

⁷⁹ *Ibid* at 8.

⁸⁰ Hansell LLP, 'Legal Opinion: Putting Climate Change Risk on the Boardroom Table' (June 2020) <<https://www.hanselladvisory.com/content/uploads/Hansell-Climate-Change-Opinion.pdf>>.

⁸¹ *Ibid* at 20.

adopting them by major Canadian companies, stating that “by supporting these standards, the Government aims to raise firms’ awareness of the importance of tracking, managing and disclosing material climate-related risks and opportunities in a consistent and comparable way.”⁸² Large companies that wish to access the federal government’s bridge financing credit relief for hardship caused by the COVID-19 pandemic must report annually on climate risks in line with the TCFD recommendations so long as the loans remain outstanding.⁸³

Practical Implications for Directors

Given that Canada has adopted a stakeholder perspective on directors’ obligations, both by statute and by opinions of the Supreme Court of Canada, given the CSA’s assertion that material climate risks need to be disclosed under current law, and given that regulators have become increasingly emphatic regarding the need for companies and their directors to adopt climate resilience measures in business practices and disclosure, well-counselled boards will:

- a) delegate climate risk identification and evaluation to a clearly-identified team in management that reports directly to the CEO and board, always keeping in mind that directors retain overall fiduciary responsibility for oversight of identification and management of climate-related risks and opportunities⁸⁴;
- b) put on the agenda for the board within 3 or 6 months a process to initiate the development of a climate transition roadmap to 2050 with transparent carbon neutrality or reduction targets, with clear interim targets to 2040, 2030 and the current rolling multi-year strategic plan, and periodically thereafter report back to the board;
- c) delegate to the appropriate committee(s) of the board, such as risk, audit, legal and governance, scenarios/strategy, nominations/remuneration, or sustainability/corporate responsibility, the task of translating the long-term strategy into a clear decision-making process for each aspect that is relevant to each committee; and

⁸² Canada Government, Budget 2019, <<https://budget.gc.ca/2019/docs/plan/anx-04-en.html>>.

⁸³ Justin Trudeau, *Prime Minister announces additional support for businesses to help save Canadian jobs*, Press release (11 May 2020) <<https://pm.gc.ca/en/news/news-releases/2020/05/11/prime-minister-announces-additional-support-businesses-help-save>>.

⁸⁴ Janis Sarra, with contributing authors Roopa Davé, Meghan Harris-Ngae, and Ravipal Bains, Canada Climate Law Initiative, *Audit Committees and Effective Climate Governance, A Guide for Boards of Directors*, (December 2020) <<https://law-ccli-2019.sites.olt.ubc.ca/files/2020/12/CCLI-Guide-for-Audit-Committees-on-Effective-Climate-Governance.pdf>>.

- d) discuss with disclosure counsel, to develop an external engagement and communications plan and ensure rigorous securities disclosure.

Contributors: Dr. Janis Sarra, Professor of Law, University of British Columbia, Canada Climate and Law Initiative and CCLI



Chile

The Financial Markets Commission (*Comisión para el Mercado Financiero*, or CMF) issued a strategy on September 25, 2020 to address climate change in the financial markets. The main objective of this strategy is to promote the disclosure of information related to climate change, as well as to promote the development of a green financial market and integrate climate risks into the risk assessments required of listed companies.

In this regard, the CMF recognized climate change as a financial risk that financial market participants must adequately manage. The work plan proposed by the CMF includes the following:

- The creation of a Climate Change Working Group within the CMF to develop a strategic climate change initiative.
- The participation of the CMF in the Green Finance Public-Private Board of the Ministry of Finance and in the work of the International Organization of Securities Commissions (IOSCO), the [International Association of Insurance Supervisors](#), and the [Network of Central Banks and Financial Supervisors to Greening the Financial System](#) (NGFS).
- A plan to boost information disclosure through regulatory changes.
- Development of a plan to promote a green financial marketplace.
- The integration of climate risks into risk assessments. In the short term, this involves defining an international best practice framework for climate risk assessment, monitoring and management (such as the TFCO Recommendations, which are expressly mentioned) based on the partnerships the CMF has built.

Directors' Duties and Climate Change

Law No.18046, known as the Corporations Law, establishes certain fiduciary obligations for members of boards of directors to duly perform their management functions. Among these fiduciary duties, applicable to listed and non-listed entities, are the duty of care, loyalty, confidentiality, information, and accountability.

Chilean *General Environmental Law No.19300* establishes a general legal statute for environmental damage in Chile in its article 51. In relation to the liability of directors and officers, Chile does not have a systematic framework regulating criminal liability for environmental damage.

However, Chile's regulation on securities and corporations does establish specific duties and levels of responsibility that directors must meet in acting as the governing body of a corporation. Firstly, *Law No.18046* establishes the liability of the board of directors as judicial and extrajudicial representatives of a corporation, along with their civil, administrative and criminal liability for acts or omissions of the corporation acting as a legal entity. Additionally, article 133 extends such liability to officers, establishing their joint and several liabilities for any damages caused to the company, the shareholders or third parties, in breach of *Law No.18046*, its Rules (contained in Ministry of Finance Supreme Decree No.702 of 2011) and the company by-laws.

Also, listed entities are obliged to respond to certain corporate governance recommendations designed by the CMF that are contained in General Rule No.385. This rule recommends the disclosure of information on certain corporate governance practices in public companies.

These practices must be applied on a "comply or explain" basis: companies are not required by law to apply them, but they must disclose which ones have been adhered to and which have not and why.

Among the recommendations included in General Rule No.385 that every board of directors must comply with or explain, there are references to the international reporting standards established by the [International Council on Integrated Reporting](#) (IIRC) and the [Global Reporting Initiative](#) (GRI).

Directors' Disclosure Obligations and Climate Change

The CMF's General Rule No.30 requires that listed entities periodically publish an annual report covering the information required in the mentioned General Rule.

General Rule No.385 contains a section on the application of processes to manage and control economic sustainability and the social and environmental risks to which listed companies are exposed.

In accordance with international standards established by entities such as the IIRC, the GRI, and IOSCO, in 2019, a draft amendment to General Rule No.30 was unveiled that includes relevant environmental, social, and corporate governance (ESG) in the annual reports of listed companies.

In particular with respect to the environment, the proposed amendment to General Rule No.30 requires entities to disclose information that enables investors to evaluate the impact that the entities have on the environment, including environmental initiatives, investments and targets related to consumption and production of materials, energy and waste generated by

their operations, the total percentage of non-renewable energy sources used, and the policies adopted to reduce greenhouse gas (GHG) emissions.

The announcement of this amendment to General Rule No.30 is pending and is expected to take place in 2021, which would mean that listed companies will report the above-mentioned GHG indicators in the first quarter of 2022.

Contributors: Franco Acchiardo, Grasty Quintana Majlis Chile

Grasty Quintana Majlis
in association with CLYDE&CO



European Union

In 2018, the European Commission adopted an Action Plan on Sustainable Growth to identify future legislative steps on climate change.⁸⁵ The Commission drew renewed attention to the concept of the 'carbon bubble', stating that: "Between 60 and 80 percent of the coal, oil and gas reserves of publicly-listed companies are 'unburnable' if the world is to have a chance of keeping global warming well below 2°C and as closely as possible to 1.5°C, as agreed at the COP21 in Paris.[...] a very substantial source of global systemic risk [...] is currently embedded within EU and global financial markets".⁸⁶

Directors' Disclosure Obligations and Climate Change

With specific reference to corporate law, the Commission addressed the climate change issue by imposing a disclosure obligation on large corporations (non-financial corporations with over 500 employees) and banks and insurance companies of any size. This was defined by *European Directive (EU) 2014/95*, also known as the Non-Financial Reporting Directive (the Directive) – in force since 2018 – and required the publication, either in the management report or in a separate report, of information on the impact of corporate activity on, among other factors, "environmental matters", i.e. the "short-term, medium-term and long-term implications" "based on the expected impact of science-based climate change scenarios on corporate strategies and activities"; this information is to be made available in the so-called "non-financial statement". The Directive does not formally require adoption of disclosure policies in the non-financial statement, but in cases where corporations do not adopt any such policies, their non-financial statement "shall provide a clear and reasoned explanation for not doing so".⁸⁷

Accordingly, boards of directors of all affected EU-based corporations must, in the first instance, analyse whether the short, medium and long-term implications of climate change could have any impacts on their corporate strategies and activities, and if so, evaluate such impacts. If it is determined that there is no impact, this must be disclosed in the non-financial statement, clarifying the precise reasoning underpinning this conclusion. If impacts have been identified and evaluated, they must be disclosed together with the measures adopted by directors to manage such impacts, unless they elect not to pursue any policy with reference to climate change – in which

⁸⁵ Regulation (EU) 2018/1999 of the European Parliament and of the Council on the Governance of the Energy Union and Climate Action planning 2030 targets and a transition to a climate neutral economy of 11 December 2018, L 328/1.

⁸⁶ Committee on Economic and Monetary Affairs of the European Parliament Draft Report, 2 February 2018.

⁸⁷ Art. 1(1) inserting Art. 19a (1) EU Directive 2014/95.

case a clear and reasoned explanation of such a decision must be reported as well. The information is organised around four pillars:

- the business model;
- policies and due diligence;
- the outcomes of such policies; and
- risks and their management.⁸⁸

In June 2019, the types of climate-related information to be included in the non-financial statement were specified through non-binding Guidelines issued by the European Commission (the Guidelines).⁸⁹ In particular, these clarify the scope of the climate information – which is not limited to the impact that climate change poses to the business (referred to as outside-in impacts) but rather includes the impacts of the business' activities on the climate as well (inside-out impacts), known as “double materiality”. The Guidelines specifically integrate the recommendations of the [Task Force on Climate-related Financial Disclosure \(TCFD\)](#), and are inspired by the proposals of the Commission's [Technical expert group on sustainable finance](#) (TEG).⁹⁰ The seven key principles set out in the Guidelines state that information shall be:

- material;
- fair;
- balanced and understandable;
- comprehensive but concise;
- strategic and forward-looking;
- stakeholder-oriented;
- consistent and coherent.

⁸⁸ Art. 1(1) inserting Art. 19 a (1), EU Directive (EU) 2014/95.

⁸⁹ European Commission Communication, 'Guidelines on Non-financial Reporting: Supplement on Reporting Climate-related Information', 2019/C 209/1 (20 June 2019) <https://ec.europa.eu/finance/docs/policy/190618-climate-related-information-reporting-guidelines_en.pdf>.

⁹⁰ In January 2019, the European Commission set up a Technical expert group on sustainable finance (TEG) to assist it in developing, in line with the Commission's legislative proposals of May 2018: an EU classification system – the so-called EU taxonomy – to determine whether an economic activity is environmentally sustainable; an EU Green Bond Standard; methodologies for EU climate benchmarks and disclosures for benchmarks; and guidance to improve corporate disclosure of climate-related information.

The Guidelines are aimed at fostering best practice in climate reporting and are very detailed, despite acknowledging the benefits of companies taking a flexible approach. They also encourage reporting of climate-related information to be integrated with other financial and non-financial information. Taking into account the TCFD recommendations, they identify typical climate-related risks and opportunities that should be considered across the whole value chain, both upstream (e.g. suppliers) and downstream (e.g. customers).

Directors' Duties and Climate Change

The Directive does not expressly refer to directors' duty of skill and care in relation to climate change. However, in all European jurisdictions, directors are obliged to oversee the company in compliance with the duty of care and loyalty. The apparent silence of the Directive in respect of directors' duties is in fact deceptive: by requiring disclosure on, among other factors, climate-related risks and opportunities, the Directive effectively sets a clear and robust standard for how the board must govern climate change. It presumes an understanding of, and assessment by, the board of the impact of climate change on the company and likewise of the company on the climate.

In particular, the description of the business model – which is one of the four pillars of the reporting framework – assumes that the board of directors has developed a corporate strategy that takes account of climate change, among other factors, in the short, medium and long term. This is a time horizon that is notably longer than the one boards usually consider in strategic planning, and to the extent it takes full account of all risks and opportunities, it has significant implications for financial planning, in terms of both capital expenditures and revenues. The core issue is whether the company's business is resilient in different climate change scenarios (ranging from 1.5°C average increase over pre-industrial temperatures to business-as-usual, given the high degree of uncertainty surrounding regulatory policy, technology and physical impacts), and it falls to the board of directors to make these determinations.

In addition, the disclosure requirement on policies and due diligence processes – the second pillar of the reporting framework – calls for the board of directors, within its duty of oversight, to institute effective internal controls as regards climate factors. The same duty of oversight likewise applies with respect to the third pillar of the reporting framework: disclosure of the metrics and targets that underpin the climate strategy, which the board must define and the delivery of which it must oversee.

The fourth pillar of the reporting framework is disclosure and management of top risks: the board of directors is ultimately responsible for the company's risk management processes, and in order to properly consider climate-related risks, is expected to assess them over the short, medium

and long-term. The board is expected to identify and fully disclose material risks and opportunities, in line with the recommendations of the TCFD, which are echoed in the European Commission Guidelines of 2019. Even though these Guidelines are not binding, they represent the most up-to-date climate reporting standard available. It follows, therefore, that, in order to fulfil their duty of skill and care – which, in all Member States, includes the duty to be fully informed – directors must properly understand and consider climate-related risks and the processes to manage them.

Due to its very nature, climate-related information forces directors to reason in terms of medium and long-term horizons, because the impacts of climate change extend over long periods and cannot be fully understood and assessed by focusing on the typical three- to four-year business planning cycle. This holds even when a jurisdiction does not explicitly contemplate the long term in the provisions addressing directors' duties. Because of the disclosure requirements under the Directive, effective climate governance means boards are naturally compelled to adopt a long-term perspective in managing the company.

Therefore, although billed as disclosure legislation, the Directive effectively has an enormous impact on the manner in which the duty of skill and care are to be interpreted and acted upon: disclosure on climate implies a robust process for identifying and managing risks and opportunities, and thus carries with it the implied directors' duty properly to manage these risks and embed these opportunities when defining the medium and long-term strategy of the company.

It is therefore through the backdoor of disclosure that climate change has penetrated the management of big European corporations across all industries. As for enforcement, under the Directive, Member States hold responsibility for determining and enforcing sanctions for non-compliance with disclosure requirements, and regulations vary from one Member State to another. For example, in the U.K. and Germany, it is a criminal offence for directors not to prepare or publish the statement of non-financial information, and not to disclose the actions taken in relation to each area (i.e. including climate change) without giving a justification. In Italy, the sanction is an administrative monetary penalty applied to those who verify the non-financial statement. In France, the only consequence for non-compliance is that any interested party may send a request to a judge for summary proceedings asking for the information to be provided; if the application is granted, the directors are liable to pay the penalty and procedural costs.

Statutory audit boards and audit firms provide an additional lever to drive the effectiveness of climate-related disclosure, insofar as they are required to check whether the non-financial statement or separate report have been provided, although as of yet, their oversight does not extend to its actual contents. However, Member States also have the option of requiring that

the information contained in the climate disclosure statement be verified by an independent assurance services provider.

Obviously, under general principles of law and procedures of each Member State, in addition to the specified sanctions, directors' civil liability for damages applies in cases of material misstatements or breach of the duty of skill and care. Since the legislation is very recent, there is no case law yet to gauge its practical application.

Another relevant development is Proposal N.2021/0104 (COD): Corporate Sustainability Reporting Directive (CSRD). In order to enable the transformation of the EU into a modern, resource-efficient and competitive economy with zero net emissions by 2050,⁹¹ as envisioned in the European Green Deal and the 2020 Work Programme, the European Commission had committed to propose a revision of *European Directive (EU) 2014/95*. As a result, on 21 April 2021, it issued Proposal N.2021/0104 (COD), also known as the Corporate Sustainability Reporting Directive Proposal, which aims to align sustainability reporting requirements with the Sustainable Finance Disclosure Regulation and the Taxonomy Regulation.⁹² The Proposal addresses the following:

- it extends the scope of reporting requirements to additional companies, including all large companies and listed companies (listed micro-companies are given until 1 January 2026);
- it requires full assurance of sustainability information by external auditors;
- it specifies in more detail the information that companies should report, and requires them to report in line with mandatory EU sustainability reporting standards; and
- it requires all information to be published as part of companies' management reports, and disclosed in digital, machine-readable format.

In addition, reporting should address:

- the resilience of the business model and strategy to sustainability-related factors;

⁹¹ On 4 March 2020, the Commission adopted the Proposal for a Regulation of the European Parliament and of the Council establishing the framework for achieving climate neutrality and amending *Regulation (EU) 2018/1999* (European Climate Law) (2020/0036 (COD)), proposing to make the objective of climate neutrality by 2050 legally binding on the EU.

⁹² *Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on sustainability-related disclosures in the financial services sector; 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.*

- opportunities related to sustainability;
- plans to align the business model and strategy with the transition to a sustainable economy, defined as limiting the rise in global average temperature to 1.5°C above pre-industrial levels, in line with the Paris Agreement;
- stakeholder engagement practices and their implications for the business model and strategy;
- implementation of the strategy as it relates to sustainability;
- sustainability-related targets and progress achieved against them;
- the role of functional areas and business units, as well as of the board, whether one-tier or two-tier as per local practice in different Member States, with regard to sustainability;
- principal actual or potential impacts related to the company's broader value chain, and any action taken and results achieved to prevent, mitigate or remediate negative impacts; and
- indicators to measure and report on the above.

In addition, the European Commission will adopt sustainability reporting standards regarding: climate change mitigation and adaptation, water and marine resources, resource use and the circular economy, pollution, and biodiversity and ecosystems. In case of infringements of these provisions, Member States are required, at a minimum, to provide for the following administrative measures and sanctions: a public statement identifying the wrongdoer; an order requiring the wrongdoer to cease the conduct and to desist from its repetition; and administrative pecuniary sanctions. These provisions are expected to enter into force in 2023, following final approval by the European Parliament.

Additional provisions for banks: In addition to the foregoing, directors of European banks (regardless of size) shall consider the [Guide on climate-related and environmental risks](#) issued by the European Central Bank in November 2020, which sets out thirteen supervisory expectations relating to risk management and disclosure of climate risks. These all fall within the board's duty of oversight, and consist of:

- understanding the impact of climate-related risk on the business over the short, medium and long term, in order to make informed strategic and business decisions;
- integrating climate risk when developing and implementing the bank's strategy;

- considering climate risk in the context of the overall business strategy and objectives, and embedding it within the risk management framework;
- ensuring the bank's setting of risk appetite framework properly accounts for climate risk;
- ensuring responsibility for climate risk is properly allocated to management within the organizational structure;
- incorporating aggregate climate risk data within internal reporting process so as properly as to reflect the bank's exposure;
- identifying, quantifying and integrating climate risk within the overall capital adequacy framework;
- embedding climate risk assessment within the bank's credit risk management process at all relevant stages (from credit-granting to portfolio-monitoring);
- integrating climate risk in the assessment of business continuity, reputation and liability;
- ongoing monitoring of the effect of climate risk on the bank's market positions and future investments, and incorporating climate risk into stress-testing methodology;
- evaluating, and where appropriate revisiting, the bank's stress testing methodology to ensure that climate risk is included in baseline and adverse scenarios;
- assessing whether climate risk could cause net cash outflows or depletion of liquidity buffers; and
- publishing meaningful and material information and key metrics in accordance with the above-referenced European Commission Guidelines of 2019 and therefore aligning with TCFD Recommendations.

The ECB will follow up in 2021 by asking banks to conduct a self-assessment against these thirteen supervisory expectations. In 2022, the ECB will carry out a full supervisory review of banks' climate practices under the SREP (Supervisory Review and Evaluation Process), with a view to taking concrete remedial measures where needed.

Practical Implications for Directors

Given the European Commission's adoption of world-leading climate disclosure regulations for non-financial companies, and additional very detailed and advanced regulations governing the management of climate risk by banks, well-counselled boards will:

- a) allocate identification of climate risks and opportunities and their evaluation to a clearly-identified team in management that reports directly to the board;
- b) put on the agenda for the board to review, within 3 or 6 months, a process to initiate the development of a climate transition roadmap to 2050, with transparent carbon neutrality targets, clear interim targets to 2040, 2030 and near-term within the current rolling multi-medium and long-term targets, and at least annually thereafter report back to the board. With reference to banks, boards should oversee and approve the development of an action plan that aligns with the above-referenced thirteen supervisory expectations by 15 July 2021 and ensure its submission to the ECB;
- c) ensure that all relevant departments, such as legal and compliance, risk management, scenario-planning, strategy, audit, procurement, human resources, government relations, investor relations, stakeholder relations, reach a clear understanding of their functional contribution to the design and delivery of the company's climate transition plan, coordinate their efforts under the leadership of the CEO, and are jointly accountable to the board;
- d) allocate to the appropriate committee(s) of the board, such as risk, audit, governance, scenarios/strategy, nominations/remuneration, or sustainability/corporate responsibility, the task of translating the long-term strategy into a clear decision-making process for each aspect that is relevant to each committee before its final approval by the board as a whole; and
- e) discuss with disclosure counsel, in order to develop an external engagement and communications plan.

Contributors: Dr. Sabrina Bruno, Full Professor of Comparative Corporate Law, University of Calabria and Luiss G.Carli



France

This section is to be read in conjunction with the above EU section, and focuses specifically on rules under French law regarding director's duties and obligations as they pertain to climate change.

There are an increasing number of cases before the French authorities demonstrating rising awareness of climate change. More and more judicial actions are being initiated against the French government or French corporations in this area. A recent illustration is the so-called "case of the century" (*Affaire du siècle*), where the Paris Administrative Court found the French government liable for ecological damage due to its inability to comply with its commitments to meet certain targets for reducing greenhouse gas emissions.⁹³ Further, several actions were initiated, mainly by associations and NGOs, against French corporations for alleged breach of their *devoir de vigilance* (see below) under French law; the claimants aim to obtain from French courts an injunction to compel such corporations either to put in place or to enhance their vigilance plan (*plan de vigilance*) in order to meet the greenhouse gas emissions target set by the government under the Paris Agreement.

French law has developed several mechanisms (obligations and incentives) to ensure that companies take environmental issues, including climate change, into greater consideration when conducting their business and interacting with third parties. French companies are subject to a wide range of international and domestic legal norms related to climate change. The following summary focuses on the main legal provisions applicable to French companies and/or their board directors.

Directors' Duties and Climate Change

Requirement to take into account social and environmental factors: Since the enactment of the PACTE Law,⁹⁴ the French Civil Code specifies that all French companies should be managed in the interest of the corporation, taking into consideration the social and environmental issues associated with their activities.⁹⁵ Failure to comply with this new provision does not render the company's acts or deliberations void. However, although we are not aware of any judicial decisions rendered on this basis at the time of drafting, failure to take social and environmental issues into consideration may trigger a liability on the part of directors, under the terms of general civil liability. In addition, an inadequate understanding of social

⁹³ Paris Administrative Court, 3 Feb.2021, nos 1904967, 1904968, 1904972, 1904976/4-1.

⁹⁴ *Law of 22 May 2019 related to the growth and transformation of businesses*, i.e., the so-called PACTE Law.

⁹⁵ Article 1833 of the French Civil Code, as amended.

and environmental risk factors may also constitute a valid reason to remove a director.

Corporate purpose (*raison d'être*): The PACTE Law also created the possibility for any company to specify a corporate purpose, or *raison d'être*, in its articles of association. French law defines the *raison d'être* as follows: "the principles adopted by the company and for the respect of which it intends to dedicate resources in the conduct of its business".⁹⁶ In essence, the *raison d'être* is characterised by the expression of a public interest purpose that transcends the sole pursuit of short-term profits.

Furthermore, the French Commercial Code specifically requires the board of directors and the management board of a limited company (*société anonyme*) to take into consideration "the company's corporate purpose, if any."⁹⁷ These provisions define the obligations of directors in terms of serving the long-term interests of the company. As such, a corporate purpose can serve as a framework for strategic decision-making.

Directors' Disclosure Obligations and Climate Change

Non-financial reporting: As laid out in the EU section above, the EU Non-Financial Reporting Directive, in force since 2018, defines a series of reporting requirements that have been translated into French law.⁹⁸ Specific non-financial reporting obligations apply to (i) French listed companies with more than 500 employees and more than EUR 40 million of net turnover or a total balance sheet of EUR 20 million, and (ii) non-listed French companies with more than 500 employees and more than EUR 100 million of net turnover or a total balance sheet of EUR 100 million. Companies must include a statement of non-financial performance (*Déclaration de Performance Extra-Financière* or DPEF) in the management report. This statement must include a presentation of the company's business model, an analysis of the main risks associated with the company's activities, a description of the policies and mitigation measures taken in response to such risks, and the results of these measures, including performance indicators.⁹⁹ The DPEF must also describe how the company takes into consideration the social and environmental impacts of its activity. More specifically, it must include information related to the company's contribution to the causes of climate change, through both its operations and the use of the goods and services it provides.¹⁰⁰ If the management report does not include this DPEF, any person having a legitimate interest may request that the French Courts enjoin the board of directors or management board (as applicable) to provide such information, and subject it to a daily fine, if

⁹⁶ Article 1835 of the French Civil code, as amended.

⁹⁷ Articles L.225-35 §1 and L.225-64 §1 of the French Commercial Code, as amended.

⁹⁸ Article L.225-102-1 of the French Commercial Code.

⁹⁹ Article R.225-105 of the French Commercial Code.

¹⁰⁰ Article L.225-102-1, III §2 of the French Commercial Code.

deemed appropriate. If the judge grants such a request, the said fine and costs of the proceedings must be borne by the directors or members of the management board, individually or jointly as the case may be.¹⁰¹

New disclosure obligations regarding the governance system of financial market participants have just been published¹⁰² as the French implementation of article 3 of the Sustainable Finance Disclosure Regulation (SFDR). They cover the following: (i) knowledge, skills and experience of the entity's governance bodies, including administrative, supervisory and management bodies (e.g. board of directors), and oversight of the integration of ESG criteria within the investment policy and strategy of the entity and its controlled entities (e.g. level of oversight and associated process, reporting of results, skills); (ii) inclusion of sustainability criteria in the remuneration policy, and disclosure of the criteria linking remuneration with key performance indicators; and (iii) integration of sustainability criteria in the articles of association (a.k.a. bylaws) of the board of directors or supervisory board.

Corporate duty of vigilance: The French corporate duty of vigilance (*devoir de vigilance*)¹⁰³ entails a legally-binding obligation for French parent companies to identify and prevent adverse human rights and environmental impacts resulting from their own direct activities, including from the activities of the companies they control, as well as indirectly from the activities of the subcontractors and suppliers with which they have an established commercial relationship. This duty only applies to the largest companies in France (i.e. any company established in France with at least 5,000 employees within the company's head office and its direct and indirect subsidiaries, whose head offices are located on French territory; or that employs at least 10,000 people within the company and its direct and indirect subsidiaries, whose head offices are located on French territory or abroad). Such companies must assess and address the risks of serious harm to people and the planet under an annual *plan de vigilance public*. Such risks should include, where appropriate, the risks associated with climate change. Courts may impose injunctions to compel compliance with such legal reporting obligations. In addition, the company's tortious liability could be sought where its failure to adopt an appropriate *plan de vigilance* has caused harm.

Practical Implications for Directors

Despite the absence as of yet of any case law that precisely defines the scope of directors' duties or helps directors determine the scope and extent of the above-mentioned obligations, the recent changes in legislation clearly

¹⁰¹ Article L.225-102-1, VI §2 of the French Commercial Code.

¹⁰² Decree no. 2021-663 of 27 May 2021 adopted in application to article L.533-22-1 of the French Monetary and Financial Code.

¹⁰³ Article L.225-105-4 of the French Commercial Code.

indicate that French directors will have to play an increasingly important role in taking environmental issues into account. This role particularly concerns the company's contribution to climate change. In this regard, our practical recommendations are as follows:

- a) Review and, where required, adapt governance to ensure appropriate leadership at board level in relation to climate-related risks, including any adverse impacts the company may have through its activities and products, and any legal risks the company may face in this respect;
- b) Designate the department(s) that is/are responsible for monitoring, and providing ongoing advice in relation to, the ever-expanding body of laws and regulations related to climate risk management in France and abroad;
- c) Delegate climate risk identification and evaluation to a clearly-identified management team that reports directly to the CEO and board, and is responsible for bringing together all key functions, including the legal and/or compliance function, enterprise risk management, strategic planning, audit, remuneration, human resources, investor relations, stakeholder relations, etc.;
- d) Review and, where required, adapt climate-related risk management policies and processes across the company's supply chain and distribution network, including affiliates, third parties, and, more generally, stakeholders, on the basis of a solid risk assessment. In this regard, broaden and deepen the company's due diligence framework for third-party intermediaries to address climate-related risk factors;
- e) Review and, where required, adapt reporting on climate-related risk factors and the measures taken to address these risks, in line with the French Commercial Code. Introduce internal assurance processes in relation to reporting; and
- f) Hold discussions with a PR advisor, in order to develop an external engagement and communications plan.

Contributors: Guillaume Nataf, BakerMcKenzie France
Blanche Balian, BakerMcKenzie France
Clotilde Guyot-Rechard, BakerMcKenzie France

Germany

The German Federal Financial Supervisory Authority (BaFin)¹⁰⁴ requires regulated entities to manage climate risks and to integrate them into their risk management frameworks. With a guidance notice published in December 2019, updated in January 2020, BaFin has provided its supervised companies, in particular banks, insurance companies, pension funds and capital management companies, with non-binding good practice guidelines on how to deal with sustainability risks and, in particular, climate risks.¹⁰⁵

With an interim report of 5 March 2020, the Sustainable Finance Committee (SFB) of the German Federal Government has, *inter alia*, proposed to expand the application of non-financial disclosures under *Directive 2014/95/EU* (the Non-Financial Reporting Directive).¹⁰⁶ Further, according to the SFB, listed companies shall be required to apply the TCFD recommendations on climate reporting from 2022 onwards. The final report of the SFB, which was announced for September 2020, has not yet been published.

In addition and more generally, the German Corporate Governance Code (DCGK) has already established an explicit expectation that companies and their management need to be aware of their role in and responsibility vis-à-vis society. In fact, social and environmental factors are considered to be relevant for business success.¹⁰⁷ This is a clear commitment to sustainability principles.

Moreover, the German Federal Government (Bundesregierung) – in a world first for a government – has set out binding national climate targets in a *Climate Protection Act* that entered into force on 18 December 2019. The *Climate Protection Act* provides for a gradual reduction in greenhouse gas emissions compared with 1990 levels, with at least a 55 percent reduction target by the year 2030. In the long term, the Federal Government is pursuing the goal of greenhouse gas neutrality by 2050. This goal is also clearly stated in the Act.¹⁰⁸

¹⁰⁴ BaFin, 'BaFin's Sustainable Finance Conference: Financial markets and climate change' (June 2019) <

https://www.bafin.de/SharedDocs/Veroeffentlichungen/EN/Fachartikel/2019/fa_bj_1905_Tagung_nachhaltige_Finanzwirtschaft_en.html>.

¹⁰⁵ BaFin, *Guidance Notice on Dealing with Sustainability Risks* (January 2020)

<https://www.bafin.de/SharedDocs/Downloads/EN/Merkblatt/dl_mb_Nachhaltigkeitsrisiken_en.pdf;jsessionid=CAFA36097D7125E6241B7D08B04596ED.2_cid500?_blob=publicationFile&v=5>.

¹⁰⁶ Sustainable Finance-Committee of the German Federal Government, *Interim Report: The Significance Of Sustainable Finance To The Great Transformation* (2020) <https://sustainable-finance-beirat.de/wp-content/uploads/2020/03/200306_SFB-Zwischenbericht_EN.pdf>.

¹⁰⁷ Regierungskommission Deutscher Corporate Governance Kodex, German Corporate Governance Code (16 December 2019), 2

<https://www.dcgk.de/files/dcgk/usercontent/en/download/code/191216_German_Corporate_Governance_Code.pdf>.

¹⁰⁸ *Gesetz zur Einführung eines Bundes-Klimaschutzgesetzes und zur Änderung weiterer Vorschriften Vom 12. Dezember 2019* (the Climate Protection Act).

Directors' Duties and Climate Change

Germany is a civil law jurisdiction. Directors' duties are codified in the *Act on Limited Liability Companies* (GmbHG) and the *Stock Corporation Act* (AktG), and fleshed out further in case law. The AktG provides for a dual board system with different duties and responsibilities for management and supervisory board members. Whereas the management board is responsible for the day-to-day business and the company's strategic direction, the supervisory board is focused on controlling and monitoring the management board's decisions. Notwithstanding these different functions, pursuant to sections 93, 116 AktG, all board members owe the company a duty of care, duty of loyalty and duty of confidentiality, and must exercise their duties "for the benefit of the company".¹⁰⁹ The duty of care requires the directors to "exercise the diligence of a prudent and conscientious manager".¹¹⁰ Notwithstanding the wide scope of directors' duties under German law, according to the codified business judgement rule, a management board member does not breach his or her duties if, when making a business decision, the management board member could reasonably assume, on the basis of appropriate information, that he/she was acting in the best interests of the company.¹¹¹

Applying these standards to directors' duties regarding the risks resulting from climate change, BaFin has summarised in its guidance notice for regulated companies that the management board is responsible for the business and risk strategy, its implementation within the company, and its communication. Thus, as a first step, management board members are expected to understand climate risks and their potential impact on the company's business. Further, management board members are responsible for fostering an effective risk culture and institutionalising processes and systems to control and oversee the impacts and implications of climate risks, applying a short, medium and long-term perspective.¹¹² In addition, although *Directive 2014/96/EU* and its implementation in German law are silent on directors' duties, the disclosure obligations at least implicitly oblige the management board members to develop an understanding, and assess the impacts, of climate change on the business, incorporate the results in the entity's strategic plans and scrutinise and challenge the company's resilience to climate-related risks.

In Germany, there is currently a widely-observed litigation matter before the Higher Regional Court of Hamm (file no. I-5 U 15/17) based on a complaint

https://www.bgbl.de/xaver/bgbl/start.xav?startbk=Bundesanzeiger_BGBI#_bgbl_%2F%2F%5B%40attr_id%3D%27bgbl119s2513.pdf%27%5D_1605199445200.

¹⁰⁹ Sections 93 para.1, 116 para.1 AktG

¹¹⁰ Sections 93 para.1, 116 para.1 AktG

¹¹¹ Section 93 para.1 AktG

¹¹² BaFin, *Guidance Notice on Dealing with Sustainability Risks* (January 2020)

https://www.bafin.de/SharedDocs/Downloads/EN/Merkblatt/dl_mb_Nachhaltigkeitsrisiken_en.pdf;jsessionid=CAFA36097D7125E6241B7D08B04596ED.2_cid500?__blob=publicationFile&v=5.

brought by a Peruvian farmer against German energy provider RWE alleging damage due to the consequences of climate change caused by the defendant. The farmer is demanding that the defendant pay 0.47 percent of the cost of protective measures for his house and village. The farmer accuses the German company of being co-responsible for climate change through the greenhouse gas emissions it produces. The claimant believes that the consequences will cause a glacier in the Andes to melt, with meltwater threatening his house and village. In an oral hearing in November 2017, the judges considered a claim for compensation to be sufficiently pleaded as to move into the next procedural stage of evidence taking.

Directors' Disclosure Obligations and Climate Change

The German government has implemented *Directive 2014/95/EU*, which provides for disclosure obligations in a non-financial statement.¹¹³ These disclosures regard, *inter alia*, the implications of climate change for the company, including potential damage caused by the company to society through its emissions, and those experienced by the company due to physical impacts, regulatory change, technological disruption etc.; and they require the company to disclose its strategy to address them by means of the *CSR Directive Implementation Act* of March 2017.¹¹⁴ Pursuant to the new regulations in sections 289b subsequent of the *Commercial Code* (HGB), companies with more than 500 employees are obliged to include a non-financial statement in their management report. Within this non-financial statement, the company must address at least the following aspects: environmental issues (including greenhouse gas emissions, water consumption, air pollution, use of renewable and non-renewable energy), employee concerns, social concerns, human rights and its efforts to combat corruption and bribery.¹¹⁵ Further, with regard to these aspects, the non-financial statement must provide information necessary for an understanding of the company's development and performance, its position and the effect of its activities on the aspects referred to above.¹¹⁶ If the company does not adopt any measures to address one or more of these aspects, it must explain and justify this clearly in the non-financial statement.¹¹⁷ Although the implementation of *Directive 2014/95/EU* generally involves a disclosure obligation for directors regarding climate change risks and impacts, as an explicit exception, the company may, in the non-financial statement, omit any information on future developments or matters under negotiation if the directors, in their exercise of sound business

¹¹³ *Directive 2014/95/EU of the European Parliament and of the Council of 22 October 2014* <<https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:32014L0095&from=EN>>.

¹¹⁴ *Gesetz zur Stärkung der nichtfinanziellen Berichterstattung der Unternehmen in ihren Lage- und Konzernlageberichten* (CSR-Richtlinie-Umsetzungsgesetz) vom 11.04.2017.

¹¹⁵ Section 289c para.2 HGB.

¹¹⁶ Section 289c para.3 HGB.

¹¹⁷ Section 289c para.4 HGB.

judgment, determine that the information is likely to cause significant damage to the company.¹¹⁸

Under the HGB, breaches of the disclosure obligations concerning the non-financial statement are sanctioned in different ways. Misrepresentation or non-disclosure of the company's relations are subject to criminal punishment, including potential prison sentences of up to three years for board members.¹¹⁹ Moreover, omitting or incompletely preparing a non-financial statement constitutes an administrative offence, resulting in possible fines of up to EUR 10 million.¹²⁰ In the event of errors in the non-financial statement, the management board members are also considered to be in violation of their obligations under section 93 AktG, which may result in liability for damages towards the company.

As an additional ramification, the implementation of *Directive 2014/95/EU* has led to an amendment in the definition of the supervisory board's responsibilities, insofar as it gives supervisory board members the option of instructing an external party to conduct a content review of the non-financial statement.¹²¹

Practical Implications for Directors

Given that German regulators have become increasingly emphatic regarding the need for companies and their directors to adopt climate resilience measures in business practices and disclosure, and in particular the above-noted BaFin guidance to its supervised companies; the German Federal Government's GHG emissions reductions targets, and revisions to the EU's non-financial reporting directive, well-counselled boards will:

- a) delegate climate risk identification and evaluation to a clearly-identified team in management which reports directly to the CEO and board;
- b) put on the agenda for the board within 3 or 6 months a process to start developing a climate transition roadmap to 2050 with transparent carbon neutrality or reduction targets, with clear interim targets to 2040, 2030, and within the current rolling multi-year strategic plan, and periodically thereafter report back to the board;
- c) delegate to the appropriate committee(s) of the board, such as risk, audit, legal and governance, scenarios/strategy, nominations/remuneration, or sustainability/corporate responsibility, the task of translating the long-term strategy into a clear decision-

¹¹⁸ Section 289e para.1 HGB.

¹¹⁹ Section 331 HGB.

¹²⁰ Section 334 HGB.

¹²¹ Section 111 para.1 AktG.

making process for each aspect that is relevant to each committee;
and

- d) discuss with disclosure counsel, to develop an external engagement and communications plan and to oversee rigorous disclosure and accounting.

Contributors: Dr. Henning Schaloske, Clyde & Co Germany

CLYDE&CO

Hong Kong

In Hong Kong, regulators recognise the foreseeability of climate-related financial risks and are proactively addressing them.¹²² In December 2020, the Hong Kong Monetary Authority (HKMA), a member of the NGFS, announced that reporting in accordance with TCFD recommendations will be mandatory for companies in the banking, asset management, insurance and pension fund sectors by 2025.¹²³ Additionally, the HKMA recently issued a circular regarding best practices by major international banks in managing climate risks, as well as several other publications regarding green and sustainable finance.¹²⁴ The Hong Kong Securities and Future Commission (SFC) and the HKMA also co-chair Hong Kong's Green and Sustainable Finance Cross-Agency Steering Group. The Steering Group includes several government agencies and aims, amongst other things, to coordinate the management of climate and environmental risks to the financial sector and to accelerate the growth of green and sustainable finance.

In November 2020, the Chief Executive of the HKMA acknowledged that “[c]limate risk is one of the biggest threats to our planet and future generations’ and that regulators must determine how the financial sector can ‘play its part in tackling this risk’.”¹²⁵ In February 2021, speaking about the international climate finance agenda, the CEO of the Hong Kong Securities and Future Commission, warned that:

International organisations, national authorities and the private sector now have no real option other than to participate. If they do not, they risk being left behind as investments shift in favour those businesses which can properly describe how they are managing the strategic risks resulting from climate change.¹²⁶

¹²² This will be analysed in depth in a forthcoming legal opinion on directors' duties and disclosure obligations regarding climate change to be issued by Alex Stock SC and Jennifer Fan, Temple Chambers: Alex Stock SC and Jennifer Fan, *Directors' duties and climate change under Hong Kong law* (forthcoming).

¹²³ Cross-Agency Steering Group Launches its Strategic Plan to Strengthen Hong Kong's Financial Ecosystem to Support a Greener and More Sustainable Future (HKMA, Press Release, 17 Dec 2020).

¹²⁴ See HKMA, 'Range of practices for management of climate risks' (7 July 2020) <<https://www.hkma.gov.hk/media/eng/doc/key-information/guidelines-and-circular/2020/20200707e1a1.pdf>>; HKMA, 'White Paper on Green and Sustainable Banking' (30 June 2020) <<https://www.hkma.gov.hk/media/eng/doc/key-information/guidelines-and-circular/2020/20200630e1.pdf>>; HKMA, 'Common Assessment Framework on Green and Sustainable Banking' (31 December 2019) <<https://www.hkma.gov.hk/media/eng/doc/key-information/guidelines-and-circular/2020/20200513e1a1.pdf>>.

¹²⁵ Eddie Yue, 'Managing climate risks in Hong Kong' (9 November 2020) [3] <<https://www.bis.org/review/r201109b.htm>>.

¹²⁶ Ashley Alder, 'Climate change and finance: What's next for the global regulators? Climate Risk and Green Finance Regulatory Forum 2021' (11 February 2021) 5 <https://www.sfc.hk/-/media/EN/files/ER/PDF/CEO_Speech_Climate-Risk-and-Green-Finance-Regulatory-Forum-2021.pdf>.

Directors' Duties and Climate Change

Hong Kong is a common law jurisdiction. Directors' duties in Hong Kong are informed by a combination of statute (principally the *Companies Ordinance* (Cap 622)) and common law. Directors owe fiduciary duties to the company including the duty to act *bona fide* in the best interests of the company, the duty to avoid unauthorised conflicts of interest and unauthorised receipt of profits, and the duty to act for proper purposes. However, these duties have not been codified; only the common law duty to exercise reasonable care, skill and diligence has been. Section 465 of the *Companies Ordinance* provides that a director of a company must "exercise reasonable care, skill and diligence".

With respect to climate change, the two most salient directors' duties are the duty to act *bona fide* in the best interests of the company and the duty to exercise reasonable care, skill and diligence. In Hong Kong, the best interests of the company are broadly understood as being commensurate with the financial interests of the members as a whole.¹²⁷ As such, under the law of Hong Kong, directors are entitled to consider climate risks in their decision-making processes to the extent that they have, or are likely to have, an impact upon the financial interests of the company's members. In fact, directors who fail to consider climate risks may fall short of their duty to act in the best interests of the company given the prominence and foreseeability of climate-related financial risks. Notably, a failure to consider could encompass situations where climate risks were considered but not given adequate weight or considered on the basis of inadequate or incorrect information. Furthermore, in a jurisdiction such as Hong Kong where financial regulators have undertaken concerted and coordinated efforts to improve climate risk literacy and governance, the objective standard expected of directors in addressing climate risks could foreseeably be higher than in other jurisdictions.

Under the law of Hong Kong, the duty of care, skill and diligence comprises an objective and subjective element. The standard of reasonable care, skill and diligence expected is based on what could reasonably be expected of a person carrying out the functions of a director,¹²⁸ as well as the subjective knowledge, skill and experience the impugned director actually has.¹²⁹ Importantly, the subjective characteristics of the director in question can only raise the expected standard.¹³⁰

The duty of care, skill and diligence owed by directors under the law of Hong Kong is relevant to climate risks in several respects. These include:

¹²⁷ *Greenhalgh v Arderne Cinemas Ltd* [1950] 2 All ER 1120, 1126; Stefan HC Lo and Charles Z Qu, *Law of Companies in Hong Kong* (Sweet & Maxwell, 3rd edn, 2018) [8.030].

¹²⁸ *Companies Ordinance* (Cap 622) s 465(2)(a).

¹²⁹ *Ibid* section 465(2)(b).

¹³⁰ *Re D'Jan of London Ltd, Copp v D'Jan* [1994] 1 BCLC 561, 563.

- the establishment and maintenance of risk management processes;
- due diligence and informed decision making;
- supervision of management and committees;
- assessment of financial statements; and
- disclosure of material information in accordance with the Hong Kong Stock Exchange Listing Rules.

Consequently, directors who dismiss, or unduly diminish the significance of climate risks, foreseeably face personal liability on several fronts under the law of Hong Kong.¹³¹

Directors' Disclosure Obligations and Climate Change

Part XIVA of the *Securities and Futures Ordinance* (Cap 571) provides that listed corporations, and therefore their directors, have an obligation of continuous disclosure regarding information which is likely to materially influence the price of their shares in certain circumstances. Similarly, the Hong Kong Stock Exchange's (HKEX) Main Board Listing Rules require disclosure of information regarding profit forecasts, among other matters. Relevantly, such disclosure could foreseeably be precipitated by a climate-related financial risk being realised.

Under rule 13.24B (1), if an event occurs during the profit forecast period which makes the assumptions underlying the profit forecast materially different, the issuer must announce this information. Furthermore, rule 13.24B (2) provides that if there are activities outside the issuer's ordinary course of business that materially contributes to or reduces the profit stated in the profit forecast, the issuer must announce this information. In addition, rule 13.91 requires companies to furnish an annual ESG report on a comply or explain basis. In the report, it is mandatory to disclose, amongst other matters:

- the board's oversight of ESG issues;
- the board's ESG management approach and strategy, including the process used to evaluate, prioritise and manage material ESG-related issues; and

¹³¹ Ernest Lim, CCLI, *Directors' Liability and Climate Risk: Hong Kong White Paper* (2021, forthcoming).

- how the board reviews progress made against ESG-related goals and targets with an explanation of how they relate to the companies' operations.

The HKEX is also pressing for greater awareness and disclosure of climate-related financial risks as well as increased uptake of sustainable finance practices. In December 2019, the HKEX introduced new ESG requirements, requiring that issuers must, amongst other things, disclose 'significant' climate-related issues which have, or may have, an impact on the company.¹³² In December 2020, HKEX launched the Sustainable and Green Exchange (STAGE), the first of its kind in Asia. The STAGE is an online portal designed to provide greater information, access, and transparency on a wide range of sustainable green and social investment products.

As noted above, the HKMA will also require directors in the banking, asset management, insurance, and pension fund sectors to ensure that their companies provide TCFD-aligned disclosures by 2025.¹³³ Asset managers in particular are likely to face more onerous disclosure obligations. In October 2020, the SFC issued a consultation paper on the management and disclosure of climate risks by fund managers. The SFC proposes to amend the Fund Manager Code of Conduct to require fund managers to consider climate risks (defined as physical, transition and liability risks) in their investment and risk management processes and make appropriate climate risk disclosures to meet investor demand for information and to combat greenwashing. These go beyond baseline TCFD-style climate risk management and disclosure in two areas: (i) requiring quantitative disclosure by large fund managers of weighted average carbon intensity for scope 1 and 2 emissions; and (ii) encouraging fund managers to look beyond their usual investment horizon "because portfolio assets will in most cases be reinvested in similar investments", meaning risks that may not be material in the short term may become material in the medium or long term.¹³⁴

Practical Implications for Directors

Given that Hong Kong's regulators have become increasingly emphatic regarding the need for companies and their directors to adopt climate resilience measures in business practices and disclosure, and in particular

¹³² HKEX, 'Amendments to the Main Board Listing Rules: Update No.128' (2019) <<https://en-rules.hkex.com.hk/rulebook/update-no-128>>; HKEX, 'Amendments to the GEM Listing Rules: Update No.64' (2019) <<https://en-rules.hkex.com.hk/rulebook/update-no-64>>.

¹³³ HKMA, Press Release 'Cross-Agency Steering Group Launches its Strategic Plan to Strengthen Hong Kong's Financial Ecosystem to Support a Greener and More Sustainable Future' (17 December 2020) <<https://www.hkma.gov.hk/eng/news-and-media/press-releases/2020/12/20201217-4/>>.

¹³⁴ Securities and Futures Commission, 'Consultation Paper on the Management and Disclosure of Climate-related Risks by Fund Managers' (2020) <<https://apps.sfc.hk/edistributionWeb/gateway/EN/consultation/doc?refNo=20CP5>>.

the above-noted facts that the HKMA will be making TCFD disclosure mandatory for its supervised entities by 2025; the involvement of HFMA and SFC in the Green and Sustainable Finance Cross-Agency Steering Group, and new ESG requirements by the HKEX, with specific attention to climate, well-counselled boards will:

- a) delegate climate risk identification and evaluation to a clearly-identified team in management which reports directly to the CEO and board;
- b) put on the agenda for the board within 3 or 6 months a process to start developing a climate transition roadmap to 2050 with transparent carbon neutrality or reduction targets, with clear interim targets to 2040, 2030, and within the current rolling multi-year strategic plan, and periodically thereafter report back to the board;
- c) delegate to the appropriate committee(s) of the board, such as risk, audit, legal and governance, scenarios/strategy, nominations/remuneration, or sustainability/corporate responsibility, the task of translating the long-term strategy into a clear decision-making process for each aspect that is relevant to each committee; and
- d) discuss with disclosure counsel, to develop an external engagement and communications plan and to oversee rigorous disclosure and accounting.

Contributors: Dr. Ernest Lim, Associate Professor, National University of Singapore
CCLI



India

Indian financial regulators are becoming increasingly attuned to the magnitude and breadth of climate-related financial risks.¹³⁵ In its 2018-2019 'Report on Trend and Progress of Banking in India', the Reserve Bank of India highlighted that climate change poses several risks to the financial system and opined on the opportunities presented by the 'green finance ecosystem'.¹³⁶ Further, in April 2020 the Reserve Bank published a study demonstrating that climate change has had a significant impact upon the inflation of food prices.¹³⁷

In August 2020, the Securities & Exchange Board of India (SEBI) released a consultation paper recommending that India's 1,000 largest companies be required annually to furnish Business Responsibility and Sustainability Reports (BRSRs).¹³⁸ SEBI proposes that BRSRs be mandatory from the 2021-2022 financial year, requiring corporations to state whether they have any strategies or initiatives in place to address climate change, as well as any ongoing projects related to the low-carbon economy.¹³⁹

Additionally, in March 2020, India's Insurance Regulatory and Development Authority co-hosted a roundtable with the OECD and Asian Development Bank that, amongst other matters, considered the implications of climate change for insurance business models and the role of pension funds in advancing sustainable finance.¹⁴⁰

Directors' Duties and Climate Change

Indian directors' duties are largely codified in section 166 of the *Companies Act*. The most relevant duties in the context of climate change are, broadly speaking, the duties of trust and loyalty and the duty of competence. The duties of trust and loyalty include the duty to act in good faith in the best interests of the company and stakeholders, as well as the duty to avoid

¹³⁵ This will be analysed in depth in a forthcoming legal opinion on directors' duties and disclosure obligations regarding climate change to be issued by Shyam Divan SC, Ria Singhsawhney and Sugandha Yadav: Shyam Divan SC, Ria Singhsawhney and Sugandha Yadav, *Climate change and duties of company directors in India* (forthcoming).

¹³⁶ Reserve Bank of India, '2018-2019 Report on Trend and Progress of Banking in India' (2019) 17 <<https://rbidocs.rbi.org.in/rdocs/Publications/PDFs/ORTP241219FL760D9F69321B47988DE44D68D9217A7E.PDF>>.

¹³⁷ Reserve Bank of India, 'Climate Change: Macroeconomic Impact and Policy Options for Mitigating Risks' (2020) <<https://rbidocs.rbi.org.in/rdocs/Bulletin/PDFs/1CLIMATECHANGEF7C6AD14719E43DAA7FA84C1F8F1CFED.PDF>>.

¹³⁸ Securities and Exchange Board of India, 'Consultation Paper on the format for Business Responsibility and Sustainability Reporting' (2020) <https://www.sebi.gov.in/reports-and-statistics/reports/aug-2020/consultation-paper-on-the-format-for-business-responsibility-and-sustainability-reporting_47345.html>.

¹³⁹ *Ibid*, 68.

¹⁴⁰ ADBI Institute, 'OECD-ADBI-IRDAI Roundtable on Insurance and Retirement Saving in Asia' (2020) <<https://www.adb.org/news/events/insurance-and-retirement-saving-asia>>.

conflicts. Regarding the duty to act in good faith and best interests, section 166(2) of the *Companies Act* provides:

A director of a company shall act in good faith in order to promote the objects of the company for the benefit of its members as a whole, and in the best interests of the company, its employees, the shareholders, the community and for the protection of environment.

Accordingly, in discharging this duty, directors must balance various stakeholder interests under a pluralistic corporate governance paradigm. Often, the interests of these stakeholders conflate to some degree when a long-term perspective is adopted, thereby simplifying the balancing act directors must undertake.

In the context of climate risk, it is notable that the provision requires directors to act “for the protection of the environment”. Consideration of matters such as climate risk and environmental protection is not optional for directors of Indian companies. Rather, it is an obligation which, if ignored, may create significant liability risk. However, this liability risk can be reduced if directors undertake a detailed assessment of climate risk facing their company, consider expert advice where appropriate, determine strategies to address the risks, implement those strategies, and consistently review the risks and the efficacy of such strategies.

Regarding the duty of competence, section 166(3) of the *Companies Act* stipulates that directors of a company shall exercise their “duties with due and reasonable care, skill and diligence and shall exercise independent judgment”. As such, Indian directors must inform themselves sufficiently about the business of the company and its associated risks. They must also employ adequate monitoring and oversight over the management of the company. Importantly, the duty of competence is assessed objectively. Hence, an honest failure on the part of directors to account for climate risk cannot be raised as an excuse against a breach of the duty. Therefore, the duty of competence will in many cases require Indian directors to investigate and engage with climate risks. Prudent engagement will likely involve integrated risk frameworks, comprehensive disclosures and considered responses from boards.

In addition to the duty of competence, the *SEBI (Listing Obligations and Disclosure Requirements) Regulations 2015* (*SEBI LODR Regulations*) require listed companies to specify a risk management framework and large listed companies to also establish a risk management committee.¹⁴¹ These Regulations add further content to the duty of competence and raise the expected standard of risk management, and *a fortiori* climate risk management.

¹⁴¹ SEBI LODR Regulations, reg. 4(1)(f)(ii).

Directors' Disclosure Obligations and Climate Change

Indian companies may be required to make climate risk disclosures both in relation to securities issuances and their ongoing disclosure obligations. Regarding the issuing of shares, the *SEBI (Issue of Capital and Disclosure Requirements) Regulations 2009* (SEBI ICDR Regulations) mandate disclosure of several types of corporate information which are likely to relate to climate risk. For example, the SEBI ICDR Regulations require a description of the company's strategy and the environmental issues faced by the company.¹⁴² They also mandate disclosure of management's discussion and analysis of the financial condition of the company, alongside a discussion of various factors (including infrequent events or known trends or uncertainties) which may have a material adverse impact upon the company's revenue or profit.¹⁴³ Moreover, the SEBI ICDR Regulations require that a company's prospectus contain the company's material internal and external risk factors,¹⁴⁴ with climate risk likely being a foreseeable factor for many companies.

As well as disclosure with respect to share issuances, disclosure of climate risks is relevant to annual reports, continuous disclosure obligations and Business Responsibility Reporting (BRR) requirements. Notably, the annual reports of Indian companies must contain a discussion regarding the company's risk management policy and the means by which the company identifies and addresses risks that pose an existential threat to the company.¹⁴⁵ Furthermore, the report must address the company's approach to energy conservation,¹⁴⁶ and more particularly, use of alternative forms of energy and investments made in company energy conservation initiatives.¹⁴⁷

Indian companies also have continuous disclosure obligations with respect to material information to ensure the market is properly informed.¹⁴⁸ The definition of material information expressly includes information arising from the impacts of climatic events, such as flooding and fires.¹⁴⁹ Additionally, under the present BRR framework, companies must report on strategies and initiatives they have adopted "to address global environmental issues such as climate change, global warming, etc."¹⁵⁰ They must also share information about whether they "identify and assess potential environmental risks".¹⁵¹

¹⁴² SEBI ICDR Regulations, Schedule VIII, Item (VIII)(D)(1)(d).

¹⁴³ SEBI ICDR Regulations, Schedule VIII, Item (IX)(E).

¹⁴⁴ SEBI ICDR Regulations, Schedule VIII, Item (IV)(B)-(C).

¹⁴⁵ Companies Act (2013) section 134(3)(n).

¹⁴⁶ Companies Act (2013) section 134(3)(m).

¹⁴⁷ Companies (Accounts) Rules, 2014, rule 8.

¹⁴⁸ SEBI LODR Regulations, Schedule III, Part A.

¹⁴⁹ SEBI LODR Regulations, Schedule III, Part A, paragraph B(6).

¹⁵⁰ Securities and Exchange Board of India, 'Format for Business Responsibility Report (BRR)', Circular CIR/CFD/CMD/10/2015 (4 November 2015) <https://www.sebi.gov.in/sebi_data/attachdocs/1446638214636.pdf>.

¹⁵¹ *Ibid.*

Practical Implications for Directors

Given that regulators in India have become increasingly emphatic regarding the need for companies and their directors to adopt climate resilience measures in business practices and disclosure, and in particular the above-noted recognition of climate risk by the Reserve Bank of India, and SEBI's consultation on expanded climate disclosure and its current BRR requirements, well-counselled boards will:

- a) delegate climate risk identification and evaluation to a clearly-identified team in management which reports directly to the CEO and board;
- b) put on the agenda for the board within 3 or 6 months a process to start developing a climate transition roadmap to 2050 with transparent carbon neutrality or reduction targets, with clear interim targets to 2040, 2030, and within the current rolling multi-year strategic plan, and periodically thereafter report back to the board;
- c) delegate to the appropriate committee(s) of the board, such as risk, audit, legal and governance, scenarios/strategy, nominations/remuneration, or sustainability/corporate responsibility, the task of translating the long-term strategy into a clear decision-making process for each aspect that is relevant to each committee; and
- d) discuss with disclosure counsel, to develop an external engagement and communications plan and to oversee rigorous disclosure and accounting.

Contributors: Dr. Umakanth Varottil, Associate Professor of Law, National University of Singapore
CCLI



Italy

This section should be read in conjunction with the previous European Union section.

Directors' Duties and Climate Change

Italy is a Civil Law jurisdiction. Directors' duties are codified in the Civil Code (section 2392 ff.) - dated 1942, later amended in 2003 - according to which directors owe a duty to the company to manage its affairs with care, evaluated according to a subjective and objective standard. With the exception of creditors, consideration of whose interests arises when the company's assets are no longer sufficient to satisfy creditor claims, the Code does not explicitly refer to any duties regarding obligations to stakeholders. Another relevant provision is article 2381 of the Civil Code, according to which the board of directors is responsible for ensuring that the company's internal organization, administration and accounting are "adequate"; this responsibility includes, among others, the duty to ensure that the enterprise risk management system functions effectively.

Viewed alongside European Directive No.2014/95/EU (the Non-Financial Reporting Directive),¹⁵² the Italian Code's two above-noted provisions, combined with the Directive's comprehensive disclosure requirements, create a clear obligation for boards of "large"¹⁵³ Italian corporations to adopt a governance approach that is focused on the long-term and thus includes climate change. In other words, by compelling disclosure that is long term-focused, boards are obliged to take appropriate actions to support these long-term disclosures, e.g. by identifying and managing climate risks and opportunities, embedding them in long-term corporate strategy, ensuring alignment with individual investment decisions, and correctly valuing company assets. It follows that under Italian law, directors' civil liability for damages may arise in cases of misstatements, overvaluation of company assets, and breaches of their duty of care for failing to identify and/or manage climate-related risks or to consider climate-related opportunities in setting the strategy.

In addition to the Civil Code, the Corporate Governance Code – which, though not hard law, defines a set of voluntary "comply or explain" recommendations – was amended in 2020 to include an explicit reference to "sustainable success". Article 1 of the Corporate Governance Code provides that "[t]he board of directors leads the company by pursuing its sustainable success", sets corporate strategy in accordance with this principle, and oversees its implementation. The concept of "sustainable success" is defined as "the objective that guides the actions of the board of

¹⁵² See EU section above.

¹⁵³ Defined as non-financials with over 500 employees and banks and insurance companies of any size – see EU section above.

directors and creates long-term value for the benefit of shareholders, taking account of the interests of other relevant stakeholders". This echoes section 172 of the U.K. *Companies Act 2006* and is consistent with the concept of "enlightened shareholder value". That being said, the voluntary nature of the Corporate Governance Code means that breaches of this principle do not give rise to any enforceable legal liability against company directors.

Contributors: Dr. Sabrina Bruno, Full Professor of Comparative Corporate Law, University of Calabria - Luiss G.Carli (Italy)



Japan

Climate change has been recognised as a material issue affecting the sustainability of almost all companies. Japan's *Climate Change Adaptation Act* and its *Act on Promotion of Global Warming Countermeasures*, read together, create regulatory expectations that all sectors of Japanese society must make efforts to control climate change through mitigation and adaptation.¹⁵⁴

Climate change risks are increasingly being acknowledged by Japanese regulators. The Bank of Japan, as Japan's primary prudential regulator, has acknowledged that climate change poses a systemic risk to the Japanese financial system.¹⁵⁵ Japan's Ministry of the Environment Climate Change Policy Division has reported that climate-related risks can result from reassessment of the value of a large range of assets with a large volume of GHG emissions during the process of adjustment towards a lower-carbon economy, and has advised companies to engage in scenario analysis to assess the resilience of their business in the face of global warming.¹⁵⁶

Directors' Duties and Climate Change

Japan is a Civil Law jurisdiction, and the legal basis for the scope of directors' and officers' duties is set out in statute under the *Companies Act of Japan* and the *Civil Code*. Directors in Japan have three primary duties:

- a duty of loyalty,¹⁵⁷ including a requirement to act in the company's best interests, which a growing number of lawyers and regulators believe includes its long-term sustainability;
- a duty to comply with all laws, regulations, ordinances, and the company articles.¹⁵⁸ For directors of large companies,¹⁵⁹ it includes a requirement to develop systems related to management of the risk of loss to the company and any of its subsidiaries¹⁶⁰ and to establish a proper internal control system to ensure that the execution of their duties complies with the relevant laws, regulations and articles of association.¹⁶¹ In such companies, a director's duty of care will not

¹⁵⁴ Article 2(1), *Act on Promotion of Global Warming Countermeasures* (Act No 117 of 1998, as amended, 地球温暖化対策の推進に関する法律平成10年法律第117号)."

¹⁵⁵ Bank of Japan, Bank of Japan joins the Network for Greening the Financial System (NGFS) (28 November 2019), <https://www.boj.or.jp/en/announcements/release_2019/rel191128a.htm/>.

¹⁵⁶ The Ministry of the Environment, Government of Japan Climate Change Policy Division, Practical Guide for Scenario Analysis in line with the TCFD recommendations, 2nd edition (March 2020), 1-5, <http://www.env.go.jp/policy/policy/tcfd/TCFDguide_2nd_EN.pdf>.

¹⁵⁷ Article 355 of the *Companies Act of Japan*.

¹⁵⁸ *Ibid.*

¹⁵⁹ Large company is a defined term under Article 2(vi) of the *Companies Act of Japan*.

¹⁶⁰ *Regulation for Enforcement of the Companies Act*, article 100(ii), 会社法施行規則平成 18 年 2 月 7 日法務省令第 12 号 Ministry of Justice Order No 12 of February 7, 2006.

¹⁶¹ *Companies Act of Japan*, article 348,362,399-13 and 416.

be effectively performed without a proper internal control system;¹⁶²
and

- a duty of care, to the standard of a prudent manager,¹⁶³ which informs the duty of loyalty and the duty to comply with all applicable laws and regulations. If a director has met this standard, it may be a defence to personal liability for an alleged breach of the duty of care.¹⁶⁴ Likewise, if there are no “significantly unreasonable aspects” involved in the decision (known as the ‘business judgment rule’), directors will not have breached their duty of care.¹⁶⁵

Directors who neglect their duties are jointly and severally liable to the company for any resulting damages; and where directors are grossly negligent or knowingly fail to perform their duties, such directors are also liable to third parties or shareholders for the resulting damages.¹⁶⁶

Directors could breach their duty to ensure the company is obeying laws and regulations by failing to consider the *Climate Change Adaptation Act*. This duty requires that businesses endeavour to adapt to climate change in accordance with the content of their business activities, and to cooperate with governments at all levels. It therefore follows that directors have a duty to endeavour to ensure their companies take robust action to adapt to climate change. In the future, any strengthening of statutes that would require companies to set targets towards decarbonization or that require companies to disclose governance, strategy, risk management, and metrics in line with an international framework would add those duties to other duties of directors.

A failure to monitor climate change risks and climate change-related regulations could give rise to a breach of the directors’ duty of care in their oversight and management of the company if a board were to fail to set up an appropriate risk management system.¹⁶⁷ In order to comply with their

¹⁶² *Regulation for Enforcement of the Companies Act*, articles 98, 100(ii), 110-4 and 112, 会社法施行規則平成 18 年 2 月 7 日法務省令第 12 号 Ministry of Justice Order No 12 of February 7, 2006.

¹⁶³ *Civil Code of Japan* (Act No 89 of 1896, as amended, 民法明治29年法律第89号) article 644; *Companies Act of Japan* (Act No.2005, as amended, 会社法平成17年法律第86号) articles 330, 355. For English translation of Japanese Laws, see Japanese Law Translation run by the Ministry of Justice, Japan <<http://www.japaneselawtranslation.go.jp/?re=02>>. As has been suggested by the Japanese Supreme Court, the duty of care is judged to be the objective standard of what a reasonably prudent person would do in comparable circumstances (see Dan W Puchniak and Masafumi Nakahigashi, ‘Case No.21: Corporate Law – Business Judgment Rule – Derivative Action – Supreme Court, 15 July 2010’, in Moritz Bälz et al eds, *Business Law in Japan ---- Cases and Comments* (Kluwer Law International; 2012) at 223.)

¹⁶⁴ *Companies Act of Japan*, examples of where having taken due care is a defence include article 52 (2)(ii), article 120 (4), and article 213 (2)(ii).

¹⁶⁵ Supreme Court 15 July 2010 – Case No 2009 ju 183, Apamanshop Case, 1332 Hanrei Taimuzu 501.

¹⁶⁶ Katsuyuki Yamaguchi, Kaoru Tatsumi, and Mamiko Komura, ‘Corporate governance and directors’ duties in Japan: overview’ (1 May 2020), <https://www.nishimura.com/sites/default/files/tractate_pdf/ja/43281.pdf>.

¹⁶⁷ For example, under articles 423(1), 348(4), 362(5), 399-13(2), and 416(2) of the *Companies Act of Japan* and articles 98, 100, 110-2, and 114 of the *Regulation for Enforcement of the Companies Act*.

duty of care in relation to the duty of oversight, directors need to ensure that such a risk management system be proper and sufficiently capable of fulfilling the responsibilities to monitor and manage the company's business, given the likelihood and magnitude of climate risks to the company. Since the financial risks of climate change are so broadly acknowledged by governments, scientists, financial institutions, companies, investors, and civil society, it is no longer a defence for directors to say that they were unaware of the risks.

As well as potentially breaching their duty of care in respect of the duty of oversight of risks and compliance, directors could potentially breach their general duty to act with due care in the best interests of the company in failing to address climate-related risks and opportunities.¹⁶⁸ Examples of breach of the duty of care could include failure to make relevant enquiries to management regarding physical and transition risks to the business due to climate change; or failure to seek outside expertise where the directors do not possess the knowledge or expertise to devise a strategy to address climate risk. Other examples might include failure to robustly assess the assumptions underlying revenue/cost projections for climate-related disruption, and failure to ensure assets and supply chains are resilient to foreseeable physical climate risks.

Additionally, regulators are encouraging the disclosure of climate-related risks (see below). The responsibility that corporate directors therefore have to ensure adequate disclosure, combined with the expectations contained in the *Climate Change Adaptation Act* and the *Act on Promotion of Global Warming Countermeasures*, put directors in the position of having to stand by the quality of the practices that these disclosures reveal, in effect creating a clear obligation to address climate-related risks and opportunities to an adequate standard. Heightened disclosure creates a *de facto* expectation of a higher standard of care.

The duty of care for publicly-listed companies is reinforced by the Japanese Corporate Governance Code, which recommends that publicly-listed companies address ESG and other sustainability issues proactively to create value for all stakeholders over the mid- to long-term.¹⁶⁹ The Code, while non-binding, therefore offers strong normative guidance for directors to effectively manage material climate-related financial risks and opportunities. The impact of soft law such as the Corporate Governance Code has the potential to be instrumental in shifting climate governance, as

¹⁶⁸ See Yoshihiro Yamada, Janis Sarra and Masafumi Nakahigashi, Commonwealth Climate and Law Initiative, *Directors' Duties Regarding Climate Change in Japan* (February 2021) <<https://law-ccli-2019.sites.olt.ubc.ca/files/2021/02/Directors-Duties-Regarding-Climate-Change-in-Japan.pdf>>.

¹⁶⁹ Tokyo Stock Exchange, 'Japan's Corporate Governance Code Seeking Sustainable Corporate Growth and Increased Corporate Value over the Mid- to Long-Term' (as revised 1 June 2018) at 16, <https://www.jpx.co.jp/english/news/1020/b5b4pj000000jvxx-att/20180602_en.pdf>. For a discussion of early corporate law, prior to the modernization of company law, see Janis Sarra and Masafumi Nakahigashi, 'Balancing Social and Corporate Culture in the Global Economy: The Evolution of Japanese Corporate Culture and Norms' (2002) 24 *Law & Policy* 4 at 299-354.

the principles adopted by companies form part of their fundamental rules of operation.

Directors' Disclosure Obligations and Climate Change

The duty to disclose is contained in the *Financial Instruments and Exchange Act* (FIEA).¹⁷⁰ Although Japan's securities regulators have not expressly stated that companies must disclose the breadth and nature of climate-related financial risk, the FIEA requires disclosure (on a continuous and periodic basis¹⁷¹) of material business risks. These risks are often reported as 'non-financial information' in annual reports. Additionally, in January 2019, Japan's Financial Services Agency issued a Cabinet Office Ordinance on Disclosure of Corporate Affairs, which expands the FIEA requirement to include material 'forward-looking' risk. While this ordinance does not refer explicitly to climate change, the requirements align closely to the TCFD framework. Therefore, insofar as climate change is now universally regarded as posing a material business risk, it follows that the FIEA requires disclosure of risks and forward-looking risks arising from climate change. Finally, if directors detect any fact likely to cause substantial detriment to the stock company, they must immediately report such fact to the shareholders or to the company auditors.¹⁷²

Directors have overall responsibility for ensuring that a company's financial disclosures are accurate, and so may be primarily liable for misleading disclosures made to the market.¹⁷³ Both companies and directors may be subject to sanctions under financial services legislation for failure to comply with disclosure requirements. Unlike general directors' duties, disclosure pursuant to financial services law is not subject to the business judgment rule; therefore, a court will not consider whether a decision to make or omit a disclosure was "significantly unreasonable" but will focus on whether the disclosure was required by law.

¹⁷⁰ Financial Instruments and Exchange Act (Act No 25 of 1948, 金融商品取引法昭和23年法律第25号), <<https://www.fsa.go.jp/en/policy/fiel/>>.

¹⁷¹ Planning and Coordination Bureau, Financial Services Agency, 'Points to Note Regarding Article 27-36 of the Financial Instruments and Exchange Act (Fair Disclosure Rule Guidelines)', (April 2018), translation at <https://www.fsa.go.jp/en/laws_regulations/disclosure/20180206-2.pdf>.

¹⁷² *Companies Act of Japan*, article 357(1).

¹⁷³ Janis Sarra, Audit Committees and Effective Climate Governance, A Guide for Boards of Directors (CCLI December 2020), <<https://law-ccli-2019.sites.olt.ubc.ca/files/2020/12/CCLI-Guide-for-Audit-Committees-on-Effective-Climate-Governance.pdf>>.

There have also been several recent regulatory and guidance developments aimed at enhancing the disclosure of climate-related risks, including:

- In 2019, a TCFD Consortium was launched to encourage effective TCFD disclosures, supported by the Ministry of the Environment and the Ministry of Economy, Trade and Industry.
- In March 2020, the Ministry of the Environment issued practical guidance on scenario analysis in line with TCFD recommendations.
- The Japan Exchange Group, Inc and Tokyo Stock Exchange Inc have also strongly endorsed ESG disclosure, including disclosure of climate-related risks, with the publication of a 'Practical Handbook for ESG Disclosure' in March 2020.
- Finally, disclosing information beyond that which is required by law is encouraged by the Japanese Corporate Governance Code.¹⁷⁴

Practical Implications for Directors

Given that Japan's government and regulators have become increasingly emphatic regarding the need for companies and their directors to adopt climate resilience measures in business practices and disclosure, well-counselled boards will:

- a) delegate climate risk identification and evaluation to a clearly-identified team in management which reports directly to the CEO and board;
- b) put on the agenda for the board within 3 or 6 months a process to start developing a climate transition roadmap to 2050 with transparent carbon neutrality or reduction targets, with clear interim targets to 2040, 2030, and within the current rolling multi-year strategic plan, and periodically thereafter report back to the board;
- c) delegate to the appropriate committee(s) of the board, such as risk, audit, legal and governance, scenarios/strategy, nominations/remuneration, or sustainability/corporate responsibility, the task of translating the long-term strategy into a clear decision-making process for each aspect that is relevant to each committee; and
- d) discuss with disclosure counsel the most effective means of developing an external engagement and communications plan and

¹⁷⁴ Tokyo Stock Exchange, 'Japan's Corporate Governance Code Seeking Sustainable Corporate Growth and Increased Corporate Value over the Mid- to Long-Term' (as revised 1 June 2018) at 3, <https://www.jpx.co.jp/english/news/1020/b5b4pj000000jvvr-att/20180602_en.pdf>.

how best to engage in effective oversight of rigorous disclosure and accounting.

Contributors: Dr. Masafumi Nakahigashi, Professor of Law, Ritsumeikan University

Dr. Yoshihiro Yamada, Professor of Law, Nagoya University

Dr. Janis Sarra, Professor of Law, University of British Columbia, Canada Climate and Law Initiative

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Malaysia

Malaysia is a common law jurisdiction and the *Companies Act 2016* (CA 2016) codifies the fiduciary duty¹⁷⁵ of loyalty of a director, established under common law. The CA 2016 sets out certain general duties of directors. Section 213 of the CA 2016 provides that a director has a duty to exercise his¹⁷⁶ powers, at all times, for a proper purpose and in good faith in the best interests of the company,¹⁷⁷ and also to exercise reasonable care, skill and diligence with the knowledge, skill and experience that may reasonably be expected of a director having the same responsibilities and any additional knowledge, skill and experience that the director in fact has.¹⁷⁸

The Malaysian courts adopt both a subjective and objective test¹⁷⁹ – the subjective element is determined based on an assessment of the state of mind of the director,¹⁸⁰ whilst the objective element is determined by whether an honest and intelligent man in the position of the director could reasonably have believed the transaction was for the benefit of the company.¹⁸¹

Whilst there have yet to be any Malaysian court decisions expressly linking the exercise of these duties with climate-related considerations, decisions of courts in other common law jurisdictions will be persuasive authority in Malaysia, particularly where claims have been brought by shareholders and members of the public against the directors of a company for failing to factor in climate change considerations in business decisions.

In light of the above, it is imperative that directors evaluate and incorporate climate risks and considerations in their board decisions, as it can be anticipated that the Malaysian courts would likely step in to align the law with modern circumstances by expressly endorsing climate change as a key consideration for determining if a director was carrying out his duties under statute and common law to act in the best interests of the company.

If directors do not proactively take into account and mitigate against climate-related risks and information in their board decisions and in the operations

¹⁷⁵ Nallini Pathmanathan J explained in Para.219 of the High Court decision of *Petra Perdana Bhd v Tengku Dato' Ibrahim Petra Bin Tengku Indra Petra & Ors* [2014] 11 MLJ 1 that the essence of a fiduciary duty involves acting *bona fide* in the interests of the company. See also the High Court decision of *Ng Pak Cheong v Global Insurance Co Sdn Bhd* [1995] 1 MLJ 64 at page 77 in citing the dicta of the Australian decision of *Australian Growth Resources Corp Pty Ltd v Van Reesema* (1988) 13 ACLR 261.

¹⁷⁶ In this section, references to “he”, “his”, “him” and “man” are intended as referring to persons of all genders.

¹⁷⁷ Section 213(1) of the CA 2016.

¹⁷⁸ Section 213(2) of the CA 2016.

¹⁷⁹ See Paragraph 166 of the Federal Court decision of *Tengku Dato' Ibrahim Petra Bin Tengku Indra Petra v Petra Perdana Bhd and Another Appeal* [2018] 2 MLJ 177 per Azahar Mohamed FCJ.

¹⁸⁰ *Ibid*, in discussing what constitutes the subjective element of the test.

¹⁸¹ This objective element is also known as the “Charterbridge Principle”, which was elaborated by Azahar Mohamed FCJ in paras.172 and 173 of *Tengku Dato' Ibrahim Petra Bin Tengku Indra Petra v Petra Perdana Bhd and Another Appeal* [2018] 2 MLJ 177 and Zainun Ali JCA in the Court of Appeal decision of *Pioneer Haven Sdn Bhd v Ho Hup Construction Co Bhd & Anor and Other Appeals* [2012] 3 MLJ 616 at paras.239 and 240.

of the companies of which they are directors, they risk claims being brought against them for personal liability for breach of directors' duties.

Directors' Duties and Climate Change

Regulators have become increasingly emphatic regarding the need for companies and their directors to adopt climate resilience measures in business practices.

On 30 April 2021, the Central Bank of Malaysia (Bank Negara Malaysia or BNM) issued the [Climate Change and Principle-based Taxonomy](#) guidance document (BNM Guidance Document),¹⁸²¹⁸³ prepared in collaboration with the Risk Management sub-committee¹⁸⁴ of the JC3 (defined below), in which it acknowledged that climate change has significant impacts on the society, economy and financial system.¹⁸⁵ Specifically, this impact would manifest in three (3) dimensions of risk, namely physical risk (damaged property, reduced productivity and disrupted trade), transition risk (changes in legislative and regulatory framework, shift in consumer and investor behaviour) and liability risk (legal risk and claims on damages and losses).¹⁸⁶

Furthermore, a Joint Committee on Climate Change (JC3) was formed on 27 September 2019 by both BNM and the Securities Commission Malaysia (SC) with the intention of pursuing collaborative actions for building climate resilience in Malaysia whilst being guided by three (3) principal mandates, one of which is to build capacity through sharing of knowledge, expertise

¹⁸² BNM, Climate Change and Principle-based Taxonomy (30 April 2021) <<https://www.bnm.gov.my/documents/20124/938039/Climate+Change+and+Principle-based+Taxonomy.pdf>> BNM had earlier issued a discussion paper on the BNM Guidance Document on 27 December 2019 for which it received written feedback from respondents, including financial institutions, asset management companies, rating agencies and non-governmental organisations, during the consultation period. See BNM, 'Climate Change and Principle-based Taxonomy' (30 April 2021) <<https://www.bnm.gov.my/-/climate-change-principle-based-taxonomy>>.

¹⁸³ Paragraph 4.4 of the BNM Guidance Documents provides that it complements the Value-based Intermediation Financing and Investment Impact Assessment Framework Guidance Document (VBIAF Guidance Document) issued by BNM on 1 November 2019. It further provides that the VBIAF Guidance Document lays the foundation for ESG considerations in the provision of financial services to generate a positive and sustainable impact on the economy, community and environment, and that while the VBIAF is premised on Shariah tenets, the framework has universal application for financial institutions seeking to reflect ESG considerations in their governance, business strategy and operations, reporting and risk management systems. The VBIAF Guidance Document is accessible via this link:

<https://www.bnm.gov.my/documents/20124/761679/VBIAF_Final+guidance+1.11.2019.pdf/97938f34-3796-216c-14a0-54002c377e3b?t=1590725447991>.

¹⁸⁴ The committee comprises of the following entities: Bank Islam Malaysia Berhad, Bank Pertanian Malaysia Berhad (Agrobank), CIMB Bank Berhad, Etiqa Insurance and Takaful, Hong Leong Bank Berhad, Institutional Investors Council Malaysia, Malayan Banking Berhad, Nomura Asset Management Malaysia Sdn. Bhd., the SC, Standard Chartered Bank Malaysia Berhad and Zurich Insurance and Takaful. See the Preface & Acknowledgement section on page 2 of the BNM Guidance Document.

¹⁸⁵ Paragraph 1.1, page 4 of the BNM Guidance Document.

¹⁸⁶ Paragraph 5.1, page 7 of the BNM Guidance Document.

and best practices in assessing and managing climate-related risks.¹⁸⁷ It was also raised in the third meeting of the JC3 on 14 September 2020¹⁸⁸ that the COVID-19 pandemic had highlighted the far-reaching impact of similar global events and introduced a further sense of urgency to the work of the JC3 in its efforts to combat climate and environmental-related events.

The JC3 held its fourth meeting on 24 February 2021¹⁸⁹ where it reflected on the initiatives completed during 2020, such as a broad-based consultation and pilot implementation of the then discussion paper on the BNM Guidance Document, and a stock-take on disclosure practices of selected financial institutions against recommendations of the [Task Force on Climate-related Financial Disclosures](#) (TCFD).¹⁹⁰ Furthermore, the JC3 also discussed its priorities for 2021, which include developing guidance documents on risk management and scenario analysis, supporting the voluntary implementation of climate-related disclosures that are aligned with TCFD recommendations, broadening engagements with relevant stakeholders to identify and address enabling conditions for the structuring of green financial products and solutions, and deepening technical capacity-building programmes with a particular focus on climate-related disclosures, climate risk management and climate scenario analysis. It was also acknowledged that the members of JC3 are stepping up efforts to implement TCFD disclosures in phases beginning 2021.

The BNM Guidance Document provides that it is imperative that financial institutions integrate climate change considerations in all aspects of their business strategies,¹⁹¹ and also recognises that financial institutions play a pivotal role in accelerating their customers' transition towards more sustainable practices in their business operations.¹⁹² Furthermore, the BNM Guidance Document provides that a consistent and systematic classification of economic activities can facilitate and promote the channeling of financial flows to activities that support climate change and environmental objectives, and further classifies¹⁹³ economic activities into three (3) broad categories of "Climate Supporting", "Transitioning, and "Watchlist" which are structured around five (5) guiding principles¹⁹⁴ (i) "climate change mitigation"; (ii) "climate change adaptation"; (iii) "no significant harm to the environment"; (iv) "remedial measures to transition";

¹⁸⁷ BNM, 'Inaugural Meeting of Joint Committee on Climate Change' (27 September 2019) <https://www.bnm.gov.my/index.php?ch=en_press&pg=en_press&ac=4920>.

¹⁸⁸ BNM and SC, 'Joint Statement by Bank Negara Malaysia and Securities Commission Malaysia - Accelerating climate action through the financial sector' (15 September 2020) <<https://www.bnm.gov.my/-/joint-statement-by-bank-negara-malaysia-and-securities-commission-malaysia-accelerating-climate-action-through-the-financial-sector>>.

¹⁸⁹ BNM and SC, 'Towards Greening the financial Sector' (25 February 2021) <<https://www.sc.com.my/resources/media/media-release/towards-greening-the-financial-sector>>.

¹⁹⁰ TCFD, 'Final Report: Recommendations of the Task Force on Climate-related Financial Disclosures', (June 2017), ii. <<https://www.fsb-tcf.org/publications/final-recommendations-report/>>.

¹⁹¹ Paragraph 1.5 on pages 4 and 5 of the BNM Guidance Document.

¹⁹² Paragraph 1.6 on page 5 of the BNM Guidance Document.

¹⁹³ See Section 9 on pages 23 and 24 of the BNM Guidance Document for further elaboration on these categories of classifications.

¹⁹⁴ See Section 7, Part C on pages 12 to 21 of the BNM Guidance Document for further elaboration on these guiding principles.

and (v) “remedial measures to transition”.¹⁹⁵ Directors in the financial industry are therefore expressly encouraged to consider the impact of climate change in their decision-making processes. More importantly, the BNM Guidance Document will definitely have an effect on the profile of industries that financial institutions are prepared to lend to, and will see a trickle-down effect to the wider economy by encouraging a shift in funding and investments towards businesses adopting climate-resilient practices. Directors of non-financial companies would therefore also do well to incorporate such practices in their companies' daily operations.

Furthermore, the SC has issued the [Guidelines on Conduct of Directors of Listed Corporations and their Subsidiaries](#) dated 30 July 2020 (revised 12 April 2021) (SC Guidelines), which reiterate the duties under the CA 2016 for a director of a corporation to exercise his powers for a proper purpose and in good faith in the best interest of the corporation in which he sits as a board member.¹⁹⁶ The SC Guidelines further provide under Chapter 5 on group governance (which took effect on 1 January 2021¹⁹⁷) that a listed corporation and its directors must establish and ensure that the group-wide framework on corporate governance include, amongst others, managing material sustainability risks.¹⁹⁸

The [Malaysian Code on Corporate Governance](#) (updated as at 28 April 2021) (MCCG) issued by the SC has long been a tool for promoting good corporate governance practices in publicly-listed companies (PLCs).¹⁹⁹ Non-listed entities are also encouraged to adopt the MCCG in their practices.²⁰⁰ The MCCG provides that effective board leadership and oversight require the integration of sustainability considerations in corporate strategy, governance and decision-making, as sustainability and its underlying ESG issues become increasingly material to the ability of companies to create durable and sustainable value and maintain confidence of their stakeholders.²⁰¹ Furthermore, boards should, in discharging their responsibilities, ensure that the strategic plan of the company supports long-term value creation and includes strategies on the economic, environmental and social considerations underpinning sustainability.²⁰² [The Corporate Governance Guide](#) 2017 (3rd edition) issued by Bursa Malaysia Berhad²⁰³

¹⁹⁵ Paragraph 9.1, page 23 of the BNM Guidance Document

¹⁹⁶ Securities Commission Malaysia, 'Guidelines on Conduct of Directors of Listed Corporations and their Subsidiaries' SC-GL/4-2020 (12 April 2021), 4 <<https://www.sc.com.my/api/documentms/download.ashx?id=e5c77f58-2055-4d1c-82f2-79f552a67682>>.

¹⁹⁷ Page 2 of the covering pages to the SC Guidelines.

¹⁹⁸ Paragraph 5.02, Chapter 5 on page 7 of the SC Guidelines.

¹⁹⁹ Securities Commission Malaysia, 'Malaysian Code on Corporate Governance', (28 April 2021), 2 <<https://www.sc.com.my/api/documentms/download.ashx?id=239e5ea1-a258-4db8-a9e2-41c215bdb776>>.

²⁰⁰ Paragraph 2.8, page 4 of the MCCG.

²⁰¹ Introductory paragraphs, Section I: Board Responsibilities, Principle A: Board Leadership and Effectiveness, page 15 of the MCCG.

²⁰² Paragraph G1.1, Section I: Board Responsibilities, Principle A: Board Leadership and Effectiveness, page 17 of the MCCG

²⁰³ Bursa Malaysia is a listed exchange holding company with several subsidiaries, including Bursa Malaysia Securities Berhad, and is under the purview of the SC and Ministry of Finance. It is the operator and regulator of Bursa Malaysia, the Malaysian stock exchange.

(Bursa Malaysia) further elaborates on this latter point by explaining that stakeholders are now more aware of the impact that businesses have on the economy, environment and society, and therefore relevant economic, environmental and social considerations should be embedded in the company's business strategies and operations.²⁰⁴

Furthermore, directors can be found personally liable under the *Environmental Quality Act 1974* (EQA 1974) for allowing practices by its companies that are harmful towards the environment, unless such director can prove that the offence was committed without his consent or connivance, and that he had exercised all such diligence to prevent the commission of the offence.²⁰⁵ In specific relation to climate change, the EQA 1974 and certain regulations made under it generally prohibit the emission of environmentally hazardous substances into different areas of the environment above prescribed limits. For example, the *Environmental Quality (Prohibition on the Use of Chlorofluorocarbons and Other Gases as Propellants and Blowing Agents) Order 1993* was introduced under the EQA 1974 pursuant to Malaysia's ratification of the Montreal Protocol²⁰⁶ to prohibit the use of controlled substances such as chlorofluorocarbons, one of the primary greenhouse gases contributing to climate change.

Malaysia does not currently have a specific legislation on climate change. The Ministry of Energy, Science, Technology, Environment and Climate Change (MESTECC) announced in May 2019 that it would need two (2) years before a Climate Change Act could be tabled before Parliament, and that the main impact of such legislation would be to institutionalise climate change action across businesses and private sectors.²⁰⁷ MESTECC has also entered into a four (4)-year collaboration with the U.K. to engage in a scoping review to ascertain whether a Climate Change Act is required and engage in knowledge-sharing with the U.K. on the latter's experiences in adopting its own Climate Change Act in 2008.²⁰⁸ The Secretary-General of MESTECC, now called the "Ministry of Environment and Water" (MEWA), has at a summit held in September 2020 mentioned that MEWA is planning to embark on a scoping review on the need for climate change legislation, which will include private sector reporting and economic instruments. There was indication of a new Climate Change Act and revisions to be made to

²⁰⁴ Bursa Malaysia, 'Pull-Out I: Guidance on Board Leadership and Effectiveness of the Corporate Governance Guide 2017 (3rd edition)' (2017), 16 <https://bursa-malaysia.s3.amazonaws.com/reports/Consolidated_CG_Guide_3.PDF>. Given that the MCCG has been revised on 28 April 2021, we anticipate that the Corporate Governance Guide 2017 (3rd edition) may be subsequently revised. However, such revised version has not yet been published at the time of writing.

²⁰⁵ Section 43 of the EQA 1974

²⁰⁶ Department of Environment Malaysia, 'Malaysia HCFC Phase-Out Management Plan (HPMP Stage-2)' (2017-22), 11-12 <https://www.doe.gov.my/portalv1/wp-content/uploads/2017/12/Buku-HPMP-Stage-2_Part1.pdf>.

²⁰⁷ See Kenneth Tee, 'Yeo: At least 24 months for Climate Change Act to be tabled if necessary' *Malay Mail* (16 May 2019) <<https://www.malaymail.com/news/malaysia/2019/05/16/yeo-at-least-24-months-for-climate-change-act-to-be-tabled-if-necessary/1753644>>, and see also Joseph Kaos Jr., 'Malaysia hopes to learn from Britain to come up with Climate Change Act, says Yeo', *The Star* (16 May 2019) <<https://www.thestar.com.my/news/nation/2019/05/16/malaysia-hopes-to-learn-from-britain-to-come-up-with-climate-change-act-says-yeo>>.

²⁰⁸ *Ibid.*

the EQA 1974 to incorporate climate change and mandating of management and reporting of greenhouse gases.²⁰⁹ Furthermore, in a subsequent interview with a news outlet on 21 April 2021, the Secretary General of MEWA stated that a Cabinet meeting on 23 December 2020 had agreed for MEWA to develop a specific climate change legislation, and that MEWA is in the early stage of developing the climate change legal framework.²¹⁰

Directors' Disclosure Obligations and Climate Change

There are a number of disclosure requirements and initiatives specific to PLCs that need to be considered by the directors of those entities.

Chapter 15 of the Main Market Listing Requirements (updated as at 1 June 2020) issued by Bursa Malaysia Securities Berhad²¹¹ (Bursa Malaysia Securities) imposes a requirement on PLCs to ensure that their directors provide an overview of the application of the principles set out under the MCCG in the annual report of the PLCs.²¹² Furthermore, the PLCs would need to disclose the application of each of the “practices” set out under the MCCG, i.e. action items that PLCs are expected to adopt to achieve a specific outcome, during the financial year, to Bursa Malaysia Securities in the prescribed format and announce the same together with the announcement of its annual report.²¹³ As mentioned in the preceding section, the MCCG provides that directors should ensure that the strategic plan of the company include environmental considerations.

Furthermore, Chapter 9 of the Main Market Listing Requirements (updated as of 1 March 2021) issued by Bursa Malaysia Securities provides that a PLC needs to include a narrative statement of its management of material economic, environmental and social risks and opportunities (Sustainability Statement), in the manner as prescribed by Bursa Malaysia Securities, in its annual report.²¹⁴ The [Sustainability Reporting Guide 2018 \(2nd edition\)](#) issued by Bursa Malaysia Securities provides further elucidation on the

²⁰⁹ See Asila Jalil, 'Govt plans to assess the need for climate change legislation', *The Malaysian Reserve* (23 September 2020) <<https://themalaysianreserve.com/2020/09/23/govt-plans-to-assess-the-need-for-climate-change-legislation/>>.

²¹⁰ See Sim Leoi Leoi, 'Legislation to address global warming in Malaysia in the works', *The Star* (22 April 2021) <<https://www.thestar.com.my/news/nation/2021/04/22/legislation-to-address-global-warming-in-malaysia-in-the-works>>.

²¹¹ Bursa Malaysia Securities is a wholly-owned subsidiary of Bursa Malaysia and provides, operates and maintains the securities exchange.

²¹² Paragraph 15.25(1) of the Main Market Listing Requirements.

²¹³ Paragraph 15.25(2) of the Main Market Listing Requirements.

²¹⁴ Item 29, Part A, Appendix 9C of the Main Market Listing Requirements, pursuant to Paragraph 9.25 of the Main Market Listing Requirements. Paragraph 9.25(1) of the Main Market Listing Requirements provides that a PLC must set out the items under Part A of Appendix 9C in its annual report unless the following conditions are met: (a) the information has been previously announced or disclosed to shareholders pursuant to the Main Market Listing Requirements, or remains substantially unchanged from year to year; (b) the PLC publishes such information on its website and (c) the PLC discloses in the annual report, the address of its website and the place on its website where the information can be accessed.

manner of preparation and information to be included in the Sustainability Statement.²¹⁵

In its 2020 Sustainability Report, Bursa Malaysia stated that it became an official supporter of the recommendations of the TCFD in 2018.²¹⁶ Furthermore, it had in 2020 joined the United Nations Sustainable Stock Exchanges Initiative Advisory Group on Climate Disclosure, a new workstream launched in 2020 that aims to support exchanges in developing best practice guidance for issuers on climate-related disclosures,²¹⁷ and also organised a “Sustainability Thematic Workshop on Climate Change: Practical Steps in Measuring and Managing Greenhouse Gas (GHG) Emissions”, aimed at providing guidance to PLCs on measuring and managing GHG emissions using widely-recognised frameworks and standards.²¹⁸ Bursa Malaysia has also previously launched the FTSE4Good Bursa Malaysia Index (F4GBM Index) on 22 December 2014.²¹⁹ To be included in the index, companies need to meet a variety of ESG inclusion criteria.²²⁰ The PLCs included in the F4GBM Index are listed publicly on the official website of Bursa Malaysia²²¹ and are able to increase their profile and exposure,²²² whilst attracting investors who want to incorporate ESG elements into their investment decisions.²²³ Assessments are based on publicly-available data sources and therefore PLCs are encouraged to

²¹⁵ Bursa Malaysia Securities, 'Sustainability Reporting Guide 2018' (2nd edition) (2018) <[https://bursa-malaysia.s3.amazonaws.com/reports/Bursa%20Malaysia%20Sustainability%20Reporting%20Guide%20\(2nd-Edition\).pdf](https://bursa-malaysia.s3.amazonaws.com/reports/Bursa%20Malaysia%20Sustainability%20Reporting%20Guide%20(2nd-Edition).pdf)>.

²¹⁶ Bursa Malaysia, 'Bursa Malaysia 2020 Sustainability Report' (2020), 4,7,43 <https://www.bursamalaysia.com/sites/5d809dcf39fba22790cad230/assets/60409d0b39fba231285dd4c8/Interactive_PDF_BURSA_SR2020_Final_R1.pdf>.

²¹⁷ *Ibid*, 2 8, 37, 44 and 40.

²¹⁸ *Ibid* 22, 44 and 80.

²¹⁹ See Bursa Malaysia, 'Bursa Malaysia announces launch of Environmental, Social and Governance Index (22 December 2014) <https://www.bursamalaysia.com/about_bursa/media_centre/bursa-malaysia-announces-launch-of-environmental-social-and-governance-index>.

²²⁰ For further details of the criteria, see Section 6, page 12 of the FTSE4 Bursa Malaysia Index Ground Rules v2.0 (December 2020) issued by the London Stock Exchange Group plc, accessible via this link:

https://research.ftserussell.com/products/downloads/FTSE4Good_Bursa_Malaysia_Index_Ground_Rules.pdf?_ga=2.240168385.376282776.1604501061-1755973650.1601360556, to be read together with Section 6, pages 13-16 of the FTSE4 Good Index Series Ground Rules v4.2 (March 2021) issued by the London Stock Exchange Group plc, accessible via this link: https://research.ftserussell.com/products/downloads/FTSE4Good_Index_Series_Ground_Rules.pdf?_ga=2.6678256.376282776.1604501061-1755973650.1601360556

²²¹ Accessible via this link:

https://www.bursamalaysia.com/sites/5d809dcf39fba22790cad230/assets/5f30cfff5b711a0bfc0d8a01/ESG_Ratings_of_PLCs_assessed_by_FTSE_Russell_n_Index_Constituents_June2020.pdf

²²² *Ibid*. See also: https://www.bursamalaysia.com/about_bursa/media_centre/ftse4good-esg-scores-on-malaysian-public-listed-companies-now-available-on-bursa-malaysia-website and <https://bursasustain.bursamalaysia.com/droplet-details/resources/ftse4good-bursa-malaysia-index>

²²³ See: https://www.bursamalaysia.com/about_bursa/media_centre/ftse4good-esg-scores-on-malaysian-public-listed-companies-now-available-on-bursa-malaysia-website and <https://bursasustain.bursamalaysia.com/droplet-details/resources/ftse4good-bursa-malaysia-index>

ensure that high quality data and information are provided publicly on their practices.²²⁴

Contributors: To' Puan Janet Looi, SKRINE Malaysia
Francine Ariel Paul, SKRINE Malaysia



²²⁴ See Bursa Sustain, 'FTSE4Good Bursa Malaysia Index' (16 March 2018) <<https://bursasustain.bursamalaysia.com/droplet-details/resources/ftse4good-bursa-malaysia-index>>.

Mexico

"Climate change and environmental degradation constitutes a challenge at national and global levels and is a source of financial risk."

"Climate-related risks are a source of financial risk. Therefore it is within the mandate of central banks and supervisory bodies to ensure that the financial system is resilient to these risks."

"Banco de México considers it is imperative to promote, throughout the financial sector, the best assessment of climate, environmental and social risks and opportunities."

Alejandro Díaz de León, Governor of Banco de México

"The focus of the economic recovery should be on reducing social gaps and climate change."

"We need to move towards sustainable finance in order to mobilize resources to address climate change risks and achieve sustainable development goals."

"We would like Mexico to begin to mobilize capital in the medium and long term to move more quickly towards a green growth path, for banks to disseminate information on risks associated with climate change but also to evaluate the impact of climate change on their projects and portfolios."

Gabriel Yorio, Undersecretary of Treasury and Public Credit of The United Mexican States

Director's Duties and Climate Change

Director's duties and liabilities are regulated by different legal frameworks depending on whether a company is private, listed, or prudentially regulated, such as financial institutions.

A. Private companies

The *Companies Law (Ley General de Sociedades Mercantiles)* regulates corporate governance in private non-regulated companies, setting forth the role, duties, obligations, authority and liability of their directors.

Directors' liabilities pursuant to the Companies Law are threefold. Directors are liable for any breach of: (i) their obligations under the company by-laws; (ii) their obligations under applicable laws and regulation; and (iii) the obligations inherently stemming from their position as directors of the company.

Directors not only have a responsibility to comply with objective duties established in the by-laws of the company and applicable laws and regulation, but also have a fiduciary duty to comply with all those obligations inherent to their responsibility to manage the company.

Pursuant to article 142 of the *Companies Law*, directors are “*mandatarios*” of the company. Under the concept of *mandato*, an agency relationship entailing particular responsibilities between the directors and the shareholders is established.

The legal concept of a *mandatario* in commercial law is regulated by the Third Title of the Commercial Code under the concept of “*comisión mercantil*”. Pursuant to articles 286 and 287 of the *Commercial Code*, a *comisionista* must follow the instructions of its principal; in the event that there are no express instructions, the *comisionista* must consult with the principal, and if that is not possible, the *comisionista* “...shall act prudently, taking care of the business as if it was his own.” The duties of a director entail a personal responsibility and demand utmost due care.

Pursuant to article 157 of the *Companies Law*, directors “have the responsibilities inherent to their mandate”. Shareholders are the principals of the directors, who give them the mandate of managing the company. Therefore, the board of directors is ultimately accountable to the shareholders and only shareholders are entitled to demand compensation for damages caused by breaches of directors to their duties.

Mexican Courts have issued persuasive (non-binding) precedents (*tesis aislada*) that provide guidance on what may be interpreted to be the obligations inherently stemming from the position of directors. The precedents provide a test to confirm if the directors have complied with their fiduciary duties. Accordingly, it shall be deemed that directors are in compliance with their fiduciary duties (i) if they are following and complying the instructions expressly given to them, (ii) if they have no express instructions, then they shall act based on proper advice and consultations, and (iii) in case there are no express instructions and it is not possible for them to act under proper advice and consultations, then they must act prudently and with utmost due care, considering the purpose and business of the company.

The precedents further clarify that if this test is not met and there is a causal link between the conduct of the director and a damage or loss of profit of the company, then it shall be deemed that the director is liable for the damages caused as a consequence of its actions or omissions in breach of its fiduciary duties.

In view of these precedents and the development of a doctrine on the scope of the fiduciary duties of directors and in particular, those duties of diligence and care, it shall be deemed that directors are liable for any damage caused as a consequence of its actions or inactions, unless there are express

instructions by the shareholders releasing them from obligations, or if the directors can prove that they are acting based on proper advice and after having made the appropriate consultations on the manner in which they must take actions, or if the directors can prove they acted prudently and with utmost due care.

Mexican law does not establish objective parameters with regard to the scope of fiduciary duties. The scope of the directors' fiduciary duties, for example, in terms of having a long-term or medium-term perspective is relative and would depend on the industry or business in question and the specific risks to which the business is subject to.

There are certain industries and regions in Mexico that are highly susceptible to the physical effects of climate change and, therefore, any such risks shall be deemed material for both short-term and long-term decisions.

Considering that scientific research and evidence are clear on the irreversible effects of climate change, it is our opinion that directors that do not take into account the risks and opportunities resulting from the effects that climate change will have on the operations, finances and profitability of their companies are incurring in breach of their fiduciary duties, and may be held liable accordingly.

The liability of directors is contingent on the business suffering the negative effects of climate change and damages or losses caused therefrom. The foregoing might preclude directors from taking immediate action or being sensitive to their fiduciary duty in the long-term; however, this does not exempt them from having such liability.

To illustrate the foregoing, we could consider the case of the tourism sector in certain coastal areas in the south east of Mexico, where the rise of the sea levels will most likely have an important impact on the areas by 2050. In these cases, the directors of, for example, companies developing hotel infrastructure must take into account the effects of global warming and the rise of the sea levels to make decisions in the medium and long term. If the directors do not consider such an important risk in their decision making process, the shareholders may hold them accountable for the damages to the business caused by the rise of sea levels resulting from the omission in taking actions to prevent any such effects.

As it has been explained, the liability would not be triggered until such time at which the business suffers damages or losses and there is a causal link between the acts or omissions of the directors and the damages or losses. To the extent that the direct and indirect effects of climate change start to manifest in the operations, finance and profitability of business, directors would be liable if they fail to meet the test above and there is a causal link between the conduct (act or omission) of the director and damages or loss of profit suffered by the company.

The *Companies Law* does not explain what must be understood by acting prudently and with outmost due care; however, the *Stock Market Law* clarifies the terms duty of diligence and duty of care of directors, which may be applied to construe what shall be the duties of directors under the Companies Law as set forth above and in the judicial precedents.

B. Listed companies

Corporate governance in listed companies is mainly regulated by the *Stock Market Law (Ley del Mercado de Valores)*.

The *Stock Market Law* expressly regulates the duties of diligence and loyalty borne by directors of publicly-traded companies, and as explained above, the scope of the duty of diligence and duty of loyalty may be used to construe the scope and extent of the obligation of directors to act prudently and with utmost due care, as implied duties of directors.

Pursuant to the Stock Market Law:

- (i) the duty of diligence requires acting in good faith, in the best interests of the company, being duly qualified, prepared and informed regarding all those aspects that are relevant to the correct operation of the company, and using the resources and organisation of the business to achieve the greatest possible efficiency in its operation and management of financial risks; and
- (ii) the duty of loyalty refers to putting the interests of the company first at all times, including but not limited to the inherent obligation to keep company information confidential, and to make decisions devoid of conflicts of interest.

C. Regulated Companies

Corporate governance of regulated entities, such as financial institutions, is subject to specific regulation contained in the law applicable to the respective entity.

General fiduciary duties are also applicable to regulated companies in relation to their specific regulations.

As at the time of writing, there is no explicit regulation regarding the obligations of financial entities or their directors to address environmental risks, with the only exception of private pension funds (*Administradoras de Fondos Para el Retiro - AFORES*) being subject to a requirement to assess the ESG factors of their investments as of January 2022.

D. Extra-Contractual Duties

The fiduciary duties that have been described above are in all cases contractual duties, as they derive from the contractual relationship between the shareholders and the directors and, therefore, only the shareholders are entitled to demand compensation if directors breach their duties causing a financial damage to the company.

Mexican law also considers extra-contractual liability that may be attributed to the directors for a breach of the law or of good practices (*buenas costumbres*), based on article 1910 of the *Federal Civil Code*. Moreover, the Mexican Constitution provides the general obligation of the private sector to act with “social responsibility”, as it states in article 25 that “The public, social and private sectors shall concur, with social responsibility, to the national economic development...”

From the environmental perspective, Mexico has legislation that imposes sanctions on companies damaging the environment either by action or omission of their board of directors. Article 24 of the *Environmental Responsibility Federal Law (Ley Federal de Responsabilidad Ambiental)* states that companies are liable for the environmental damage caused by its managers, officers, directors and employees and any staff with control over the operations of the company if they omit or act within their authority, representing the company or when they order or agree on actions that damage the environment.

Irrespective of their contractual obligations under the by-laws of the companies in which they serve as directors, directors shall in all cases, act in accordance with good practices and assume their social responsibility.

To the date hereof, there are no judicial precedents nor guidance on what shall be deemed good practices and assuming your social responsibility.

Directors' Disclosure Obligations and Climate Change

The *Companies Law* establishes that directors must present an annual financial report to shareholders, including financial statements and information describing the financial state of the company.²²⁵ There is no explicit obligation to disclose information about potential climate risks, although such an obligation may be inferred as part of the fiduciary duty of

²²⁵ Pursuant to article 172 of the Companies Law, at least the following information must be presented to shareholders every year: an explanation of the general state of the company main policies implemented and key projects; an explanation of the accounting standards used to prepare the financial information; the updated finances of the company; a report on the changes of the general finances and assets of the company; and any note or clarification regarding the information provided.

diligence and to the extent that the risks of climate change are material to the business and purpose of the company.

In the case of listed companies, pursuant to the *Stock Market Law*, directors must disclose material information or events to the general public. The legislation does not expressly establish the obligation to disclose climate-related risks, but they must be disclosed to the extent that they are considered material events. The omission of disclosing material events, or making material misstatements, may give rise to financial sanctions.

In recent years, the Mexican stock markets and a significant number of listed companies have been active in promoting the disclosure of ESG information and adherence to recommendations of the [Task Force on Climate-related Financial Disclosures \(TCFD\)](#) and the [Sustainability Accounting Standards Board \(SASB\)](#) standards.²²⁶

As at the time of writing, ESG disclosure and adherence to the TCFD recommendations, SASB standards, or any other climate or ESG disclosure standard are voluntary.

Practical Implications for Directors

Notwithstanding the slow pace at which Mexican regulators are issuing and implementing regulation regarding the adoption of climate resilience measures in business practices and disclosures, companies must act based on their own risks analysis and scenarios to adopt climate resilience measures and disclosure to prevent potential financial damages. In this sense, well-counselled boards will:

- a) expressly determine the responsibility of the board to identify climate risk and opportunities and in its case, appoint a clearly-identified team in management to that effect reporting directly to the CEO and board;
- b) include in the agenda of the board the development of a climate transition roadmap to 2050 with transparent carbon neutrality and reduction targets, with clear interim targets to 2030 and 2040, and a current rolling multi-year strategic plan, with periodic reporting to the board;
- c) delegate to the appropriate committee(s) of the board, such as risk, audit, legal and governance, scenarios/strategy, nominations/remuneration, or sustainability/corporate responsibility,

²²⁶ Some of the companies that are supporters of the Task Force on Climate-Related Financial Disclosure and are active promoters of disclosure of climate risks are: Afore XXI Banorte, Cemex, BIVA, Citibanamex, Citibanamex Afore, Fresnillo, Orbia and Funo.

the task of translating the long-term strategy into a clear decision-making process for each aspect that is relevant to each committee; and

- d) discuss with disclosure counsel, in order to develop an external engagement and communications plan.

Contributors: Yves Hayaux du Tilly L., Nader, Hayaux & Goebel Mexico
Juan Pablo Sainz M., Nader, Hayaux & Goebel Mexico



New Zealand

Regulators in New Zealand readily acknowledge the systemic financial problems posed by climate change. The Governor of the Reserve Bank of New Zealand has highlighted that “[c]limate change is a key risk to global financial stability’ which ‘holds far-reaching implications for New Zealand’s financial system”.²²⁷ Consequently, the Governor has declared that “consideration of climate change needs to be a ‘must do’, not a ‘nice to have’”. Similarly, the Chief Executive of the Financial Markets Authority has made clear that the regulator intends to “ensure that listed issuers consider the risks (and opportunities) to their business models and profitability from climate change”.²²⁸

Directors' Duties and Climate Change

New Zealand directors' statutory duties are set out in the *Companies Act 1993* (Part 8).²²⁹ The core duties of directors include the duty to act in good faith and in the best interests of the company (section 131), to exercise powers for a proper purpose (section 133), and to exercise reasonable care, diligence and skill (section 137).

Law firm Chapman Tripp published a legal opinion in 2019 on the duties of New Zealand company directors and managed investment scheme providers regarding climate-related risks (the [Chapman Tripp opinion](#)). The opinion acknowledged that climate change is a foreseeable financial risk and must be considered by directors and fund managers in the same way as any other financial risk.²³⁰ In particular, where companies are affected by climate-related financial risk, directors' duty of care requires that they, at a minimum: identify that risk; periodically assess the nature and extent of the risk to the company, including by seeking and critically evaluating advice as necessary; and decide whether, and if so, how to take action in response, taking into account the likelihood of the risk occurring and possible resulting

²²⁷ Adrian Orr, 'Progressing Climate Action by Driving Transformational Change' (2020) *Reserve Bank of New Zealand Website* <<https://www.rbnz.govt.nz/research-and-publications/speeches/2020/speech2020-10-28>>.

²²⁸ Financial Markets Authority, 'Rob Everett speaking at the Financial Services Council Breakfast' (2020) *Financial Markets Authority Website* <<https://www.fma.govt.nz/news-and-resources/speeches-and-presentations/rob-everett-speaking-at-the-financial-services-council-breakfast/>>.

²²⁹ *Companies Act 1993*: sections 131, 133, 137. There is support in the case law that the common law duties continue alongside directors' statutory duties, i.e. unlike in some other jurisdictions such as England, New Zealand directors owe duties under both statute and judge-made law. For the strongest statement of this approach see *Benton v Priore* [2003] 1 NZLR 564 at 573. See also *Sojourner v Robb* [2006] 3 NZLR 808 at 829. This does not have practical implications for the analysis, so the primer follows the Chapman Tripp opinion and focuses on the statutory duties.

²³⁰ Sustainable Finance Forum, Chapman Tripp Legal Opinion (October 2019), 3 <<https://chapmantripp.com/media/r30jdd05/climate-change-risk-legal-opinion-2019.pdf>>.

harm. The more material the risk, the more it would be reasonably expected to be considered.²³¹

Directors' Disclosure Obligations and Climate Change

The Chapman Tripp opinion also considers directors' disclosure obligations with respect to climate-related risks. It concludes that where the company has public disclosure obligations, directors must ensure that they disclose material financial risks associated with climate change.²³² Best practice corporate governance guidance issued by the New Zealand Exchange and Financial Markets Authority is also explicit on the importance of reporting on environmental factors, including climate change.²³³

In April 2021, the New Zealand Government introduced legislation that will make TCFD-aligned climate risk disclosure mandatory for approximately 200 organisations that meet a NZ\$1 billion asset threshold, including most listed issuers, large registered banks, insurers, and managers of investment schemes, all of which are designated as "climate reporting entities".²³⁴ For licensed insurance companies that do not meet the asset threshold, they are still required to disclose if, in each of their two preceding accounting periods, the combined annual gross premium revenue of the insurer and its subsidiaries was more than NZ\$250 million.²³⁵

The draft legislation amends the *Financial Markets Conduct Act* to require climate reporting entities to annually produce 'climate statements' that are accessible to stakeholders and regulators, and must be signed off by directors.²³⁶ The Bill amends the *Financial Reporting Act* to enable the External Reporting Board (XRB) to prepare and issue climate-related reporting standards that align with the TCFD framework, including determining the extent to which entities will need to disclose greenhouse gas emissions. Entities must make disclosures in accordance with these

²³¹ *Ibid*, 4.

²³² *Ibid*, 3.

²³³ NZX, Guidance Note: Environmental, Social and Governance (December 2017), 4-6 <[https://s3-ap-southeast-2.amazonaws.com/nzx-prod-c84t3un4/comfy/cms/files/files/000/002/924/original/NZX ESG Guidance Note - 11 December 2017 %28final for publication%29.pdf](https://s3-ap-southeast-2.amazonaws.com/nzx-prod-c84t3un4/comfy/cms/files/files/000/002/924/original/NZX_ESG_Guidance_Note_-_11_December_2017_%28final_for_publication%29.pdf)>; FMA, Corporate Governance Handbook 2018, 16: <<https://www.fma.govt.nz/assets/Guidance/180228-Corporate-Governance-Handbook-2018.pdf>> ; New Zealand Corporate Governance Forum , NZ Corporate Governance Forum Guidelines (July 2015), 7: <<https://cmpartners.co.nz/wp-content/uploads/2015/02/NZCGF-Corporate-Governance-Guidelines-July-2015.pdf>>.

²³⁴ Financial Sector (Climate-related Disclosures and Other Matters) Amendment Bill, which is an omnibus Bill that will amend the *Financial Markets Conduct Act 2013 (FMCA)*, the *Financial Reporting Act 2013*, and the *Public Audit Act 2001*. Financial Sector (Climate-related Disclosures and Other Matters) Amendment Bill, <<https://legislation.govt.nz/bill/government/2021/0030/latest/096be8ed81aa816f.pdf>>. It was introduced on 12 April 2021, and passed first reading on 15 April 2021, it is now with the Parliamentary Select Committee.

²³⁵ *Ibid*, new section 461P(2), *FMCA*.

²³⁶ *Ibid*. For registered schemes, climate statements must be prepared for the separate funds of the scheme.

climate standards. The Bill details a series of behaviours that would be regarded as offences committed by companies and/or directors personally, including: a failure to comply with the new provisions on climate reporting disclosure records;²³⁷ knowingly failing to comply with an applicable climate standard;²³⁸ for directors or employees, failing to provide information or an explanation to the climate assurance practitioner;²³⁹ failing to file climate statements within four months of the climate reporting entity's balance date;²⁴⁰ and for a climate reporting entity that is required to prepare an annual report under the *Companies Act*, failing to state in its annual report that the entity is a climate reporting entity.²⁴¹

New Zealand's new mandatory comply-or-explain regime allows, per the 'explain' option, exceptions from compliance with the legislation, but only where rigorous requirements are met. It requires an entity to file a statement that it has "reasonably determined", in accordance with applicable climate standards, that the "relevant activities are not materially affected by climate change"; requires an explanation as to how the entity has reached that determination;²⁴² and requires the entity to obtain and file an assurance report from a qualified climate disclosure assurance practitioner in relation to its determination that climate risk is not material.²⁴³

The government has stated that the NZ\$1 billion threshold for climate risk reporting will ensure that 90% of assets under management in New Zealand are included within the disclosure system.²⁴⁴ The legislation passed first reading on 15 April 2021, underwent public consultation that ended in May and is now with the Select Committee on Economic Development, Science and Innovation Committee, scheduled to report to NZ Parliament by 16 August 2021. Once the *Financial Sector (Climate-related Disclosures and Other Matters) Amendment Bill* is passed, disclosures will be required for financial years commencing in 2022, meaning that the first disclosures will be made in 2023.²⁴⁵ The NZ Government has announced that it will publicly consult on possible wider private sector application after the legislation has been brought into force.²⁴⁶

²³⁷ *Ibid*, new section 461T, *FMCA*, including fines up to NZ\$50,000.

²³⁸ *Ibid*, new section 461ZC, *FMCA*, including fines up to NZ\$500,000.

²³⁹ *Ibid*, new section 461ZK, *FMCA*.

²⁴⁰ *Ibid*, new section 461ZN, *FMCA*.

²⁴¹ *Ibid*, new section 461ZO, *FMCA*.

²⁴² *Ibid*, new sections 461ZA and 461ZB, *FMCA*.

²⁴³ *Ibid*, new section 461ZB, *FMCA*.

²⁴⁴ New Zealand Government, 'New Zealand first in the world to require climate risk reporting', (15 September 2020), <<https://www.beehive.govt.nz/release/new-zealand-first-world-require-climate-risk-reporting>>.

²⁴⁵ Ministry for the Environment, Mandatory climate-related disclosures, (April 2021) <<https://environment.govt.nz/what-government-is-doing/areas-of-work/climate-change/mandatory-climate-related-financial-disclosures/>>. See also ESG Investor, 'NZ Introduces Law on Mandatory Climate Disclosures' (April 2021) <<https://www.esginvestor.net/nz-introduces-law-on-mandatory-climate-disclosures/>>.

²⁴⁶ For a discussion, see CCLI, On the Horizon – Briefing note on TCFD-aligned mandatory disclosure in New Zealand (June 2021) <<https://ccli.ubc.ca/wp-content/uploads/2021/06/On-the-Horizon-%E2%80%93-Briefing-note-on-TCFD-aligned-mandatory-disclosure-in-New-Zealand.pdf>>.

Practical Implications for Directors

Given that regulators in New Zealand have become increasingly emphatic regarding the need for companies and their directors to adopt climate resilience measures in business practices and disclosure, and in particular the above-noted recognition of climate risk by the Governor of the Reserve Bank, Government's plan to make TCFD disclosure mandatory, and the Chapman Tripp opinion on directors' duties, well-counselled boards will:

- a) delegate climate risk identification and evaluation to a clearly-identified team in management which reports directly to the CEO and board;
- b) put on the agenda for the board within 3 or 6 months a process to start developing a climate transition roadmap to 2050 with transparent carbon neutrality or reduction targets, with clear interim targets to 2040, 2030, and within the current rolling multi-year strategic plan, and periodically thereafter report back to the board;
- c) delegate to the appropriate committee(s) of the board, such as risk, audit, legal and governance, scenarios/strategy, nominations/remuneration, or sustainability/corporate responsibility, the task of translating the long-term strategy into a clear decision-making process for each aspect that is relevant to each committee; and
- d) discuss with disclosure counsel, to develop an external engagement and communications plan and to oversee rigorous disclosure and accounting.

Contributors: Dr. Janis Sarra, Professor of Law, University of British Columbia, Canada Climate and Law Initiative
CCLI



Russia

Russian laws expressly regulate only following the issues connected with climate change, including:

- prohibitions and restrictions on the activity causing harm to the environment: in particular, by means of rate-setting and regulation;
- liability measures for violations of such prohibitions and restrictions: in particular, measures of public liability of directors for violations committed by their companies, i.e. fines, disqualification, etc.; measures of private liability, i.e. compensation of damages, subsidiary liability for the company's obligations in case of bankruptcy, disciplinary liability for the improper performance of their duties as directors, per their legal and contractual obligations.

The Russian Civil Code provides for the obligation of directors to act reasonably and in good faith for the benefit of the company.²⁴⁷ However, the Code does not make explicit reference to directors' fiduciary duty in respect of climate change. To the extent that directors are held to such duties, they arise from the company itself voluntarily committing to good practice, placing responsibility for climate governance with the board and disclosing these commitments via publicly available statements and documents.

Examples of such internal documents determining corporate governance standards are as follows:

- corporate ethics (culture) codes;
- corporate governance codes;
- ESG and disclosure policies etc.

In 2014, the Bank of Russia approved the Corporate Governance Code, the implementation of which is recommended to public companies.²⁴⁸ The Corporate Governance Code is not mandatory. However, public companies are encouraged to adhere to it, and may adopt model language contained in the Code as their own, and include it in their public documents.

²⁴⁷ Russian Civil Code, article 53.1, clause 3.

²⁴⁸ Letter of the Bank of Russia "On the Corporate Governance Code" No.06-52/2463 dated 10 April 2014.

Directors' Duties and Climate Change

The Corporate Governance Code sets out the following duties of company directors:

- to assess and take into account non-financial environmental risks;
- to disclose additional information in the areas of social and environmental responsibility, in particular, the company's policies and management systems related to the environment); and
- to include in annual reports information on the company's policy in the field of environmental protection and environmental policy.

In addition, most public companies have adopted their own definitions of director duties, which they incorporate into their by-laws or other documentation that are made public. These definitions often include the following duties:

- to be guided by the principle of preventing rather than remediating environmental damage;
- to improve competencies and raise awareness amongst employees in the field of environmental best practice; and
- to take measures to reduce greenhouse gas emissions.

Russian legislation continues to develop. At present, there are several draft laws under consideration that address the regulation of companies' carbon footprints. If they are adopted, they may also affect directors' duties in the sphere of climate change.

Directors' Disclosure Obligations and Climate Change

Information regarding climate change is normally disclosed within annual reports, sustainable development reports and environmental reports.

Public disclosure generally includes:

- data on certification (*inter alia* voluntary) of products, equipment and buildings;
- corporate environmental goals and performance against them;
- environmental management systems;

- Information concerning the issuance of Green Finance instruments, such as bonds, project finance and bank loans used to finance renewable energy projects;
- resource efficiency processes and policies; and
- efforts to improve energy efficiency etc.

Given that issues connected with climate change are on the agenda of Russian public companies and their boards, it is highly recommended to adopt climate resilience measures in business practices, which may include:

- a) adopting internal documents determining corporate governance standards (ESG policies, etc.);
- b) delegating climate risk identification and evaluation to a clearly-identified management team which reports directly to the CEO and board;
- c) initiating the development of a climate transition roadmap to 2050 with transparent carbon neutrality or reduction targets, with clear interim targets for 2040 and 2030, a current rolling multi-year strategic plan, and periodical reports back to the board;
- d) delegating to the appropriate committee(s) of the board, such as risk, audit, legal and governance, scenarios/strategy, nominations/remuneration, or sustainability/corporate responsibility, the task of implementing the long-term strategy into a clear decision-making process for each aspect relevant to each committee; and
- e) discussing with the disclosure counsel, in order to develop an external engagement and communications plan.

Contributors: Nikita Shabalin, DLA Piper Russia



Singapore

In Singapore, regulators are increasingly scrutinising financial institutions' and companies' responses (or lack thereof) to climate risks and, more generally, environmental risks. In June 2020, the Monetary Authority of Singapore (MAS), a founding member of the NGFS, urged financial institutions to report the impact of material climate-related risks on their business and operations in accordance with international guidelines such as the TCFD recommendations.²⁴⁹ In October 2020, the Managing Director of the MAS opined that "Singapore has much at stake in global efforts to mitigate climate risk" and that "[f]inancial institutions cannot afford to ignore these risks".²⁵⁰

In December 2020 the MAS, in its capacity as central bank and financial regulator, issued its Guidelines on Environmental Risk Management for the banking, insurance, and asset management sectors.²⁵¹ These guidelines establish the expectation that financial institutions will assess, monitor, mitigate and disclose environmental risks, including physical and transition risks. In addition, since 2016 the Singaporean Exchange has required listed companies to furnish annual sustainability reports containing their identification and evaluation of material environmental, social and governance issues on a comply or explain basis.²⁵²

Directors' Duties and Climate Change

Singapore is a common law jurisdiction where both statute (principally the *Companies Act* (Cap 50)) and common law inform directors' duties. The *Companies Act* imposes several specific obligations on company directors. Section 157(1) of the *Companies Act* provides that directors shall "...at all times act honestly and use reasonable diligence in the discharge of the duties of his office". The assessment of reasonable diligence is an objective one, requiring investigation as to whether the director exercised the same degree of care and diligence as a reasonable director would have in the relevant circumstances.²⁵³ This duty exists in addition to the similar duty at common law to exercise care, skill, and diligence in relation to the company.²⁵⁴ Section 157(2) requires that a director not make improper use

²⁴⁹ MAS, 'Consultation Paper on Proposed Guidelines on Environmental Risk Management for Banks' (25 June 2020) <<https://www.mas.gov.sg/publications/consultations/2020/consultation-paper-on-proposed-guidelines-on-environmental-risk-management-for-banks>>; MAS, "Consultation Paper on Proposed Guidelines on Environmental Risk Management for Insurers" (25 June 2020).

²⁵⁰ "Harnessing the Power of Finance for a Sustainable Future", (October 2020) <<https://www.mas.gov.sg/news/speeches/2020/harnessing-the-power-of-finance-for-a-sustainable-future>>.

²⁵¹ MAS, 'Guidelines on Environmental Risk Management for Asset Managers' (8 December 2020); MAS, 'Guidelines on Environmental Risk Management for Insurers' (8 December 2020); MAS, 'Guidelines on Environmental Risk Management for Banks' (8 December 2020).

²⁵² Singapore Exchange Listing Rules, rr 711A and 711B.

²⁵³ *Lim Weng Kee v Public Prosecutor* [2002] 2 SLR(R) 848 at [28].

²⁵⁴ *Bristol and West Building Society v Mothew* [1998] Ch 1 at 16.

of his office or any information in that capacity to gain, directly or indirectly, an advantage for himself or another, or to cause detriment to the company.

As fiduciaries, directors also have a duty to act *bona fide* in the best interests of the company,²⁵⁵ and to avoid any action that may result in them being in a position of conflict of interests with the company.²⁵⁶ Furthermore, there are numerous offence-creating provisions in Singapore's environmental legislation that specifically provide for the directors of companies to be criminally liable for their companies' breaches of these laws.²⁵⁷

In 2021, Singaporean barrister and former Deputy Solicitor General Jeffrey Chan Wah Teck SC released a legal opinion on directors' responsibilities and climate change under Singaporean law (the [Chan Opinion](#)). Chan SC concluded that:

[A]t this time, directors in Singapore are obliged, when carrying out their responsibilities as directors, to take into account climate change and its associated risks, particularly insofar as those risks are or may be material to the interests of the company.²⁵⁸

The Chan Opinion identified that such obligations arise from the directors' duties of care and diligence and to act in good faith, as well as statutes addressing environmental sustainability and climate change. Notably, the Chan Opinion observed that directors may be held criminally liable under Singaporean environmental sustainability and climate change statutes for failing to ensure that their companies have in place principles and systems for compliance.²⁵⁹

Moreover, the Chan Opinion highlighted that the Singaporean business judgement defence will not protect a director who fails to make a conscious decision, does not exercise their judgment, or fails to properly inform themselves of the relevant facts and circumstances before undertaking a course of action.²⁶⁰ Furthermore, Chan SC posited that Singaporean law requires "at the very least" that directors consider their companies' exposure to the physical, transitional, and liability risks associated with climate change, with directors who fail to do so potentially facing criminal prosecution as well as personal liability.²⁶¹ Accordingly, the Chan Opinion

²⁵⁵ *Re Smith and Fawcett Ltd* [1942] Ch 304 at 306.

²⁵⁶ *Bray v Ford* [1896] AC 44 at 51

²⁵⁷ For example, see *Environmental Protection and Management Act* (Cap 94A, 2002 Rev Ed.) s 71(1).

²⁵⁸ Jeffrey Chan SC et al, 'Legal Opinion on Directors' Responsibilities and Climate Change Under Singaporean Law' (April 2021) at [79], <<https://ccli.ubc.ca/wp-content/uploads/2021/04/Legal-Opinion-on-Directors-Responsibilities-and-Climate-Change-under-Singapore-Law.pdf>>.

²⁵⁹ *Ibid* at [45].

²⁶⁰ *Ibid* at [76].

²⁶¹ *Ibid* at [79].

urges directors to institute governance and management processes for identifying, monitoring, managing, and reporting on climate risks.²⁶²

Directors' Disclosure Obligations and Climate Change

Companies listed in Singapore have an obligation of continuous disclosure with respect to information that is likely to have a material effect on the price or value of their securities.²⁶³ The Chan Opinion highlighted that there are numerous ways in which climate risks may have a material effect on the price or value of securities, including through:

- a) Legislative changes rendering certain company assets or activities unusable or untenable at cost (such as the phase-out of petrol and diesel vehicles);
- b) Damage caused by extreme weather events in particular geographical locales which might be especially susceptible (such as flood-prone or coastal areas);
- c) The commencement of climate change litigation against the company or one of its subsidiaries;
- d) Rising financing or insurance costs for certain company activities or assets (such as coal-fired power plants); and
- e) The exposure of its counter-parties to the above risks.²⁶⁴

Accordingly, the Chan Opinion opines that where these circumstances are present, directors ultimately hold responsibility for ensuring that their company discloses in compliance with the Singaporean Exchange Listing Rules.²⁶⁵ Singaporean companies are also required to furnish an annual sustainability report which must include material environmental, social and governance factors; policies, practices and performance; targets; sustainability reporting frameworks; and board statements.²⁶⁶ Additionally, under the *Banking Act* (Cap 19) the MAS may also require banks to publicly disclose information relating to their risk profile and risk management processes.²⁶⁷ Foreseeably, the MAS could seek information pursuant to its recently released Guidelines on Environmental Risk Management to examine banks governance of climate risks.

Regarding disclosure obligations and climate change under Singaporean law, the Chan Opinion concluded that:

[...] directors who fail to disclose physical and transition risks to the valuation of the assets and liabilities under their

²⁶² *Ibid* at [80].

²⁶³ Singapore Exchange Listing Rules, r 703.

²⁶⁴ Jeffrey Chan SC et al, 'Legal Opinion on Directors' Responsibilities and Climate Change Under Singaporean Law' (April 2021) at [64].

²⁶⁵ *Ibid* at [65].

²⁶⁶ Singapore Exchange Listing Rules, rr 711A and 711B.

²⁶⁷ Sections 10B(1) and (2), *Banking Act* (Cap 19) (see also s 26(1)).

stewardship may face various civil liabilities, even within the context of existing financial reporting standards.²⁶⁸

Consequently, a practical understanding of the financial implications arising from climate change is necessary for companies listed in Singapore to appropriately discharge their disclosure obligations.

Practical Implications for Directors

Given that regulators in Singapore have become increasingly emphatic regarding the need for companies and their directors to adopt climate resilience measures in business practices and disclosure, and in particular the above-noted recognition of climate risk by the MAS, its guidelines for Environmental Risk Management and disclosure for banking, insurance, and asset management, the Singaporean Exchange regulations regarding sustainability reporting, and the Chan legal opinion, well-counselled boards will:

- a) delegate climate risk identification and evaluation to a clearly-identified team in management which reports directly to the CEO and board;
- b) put on the agenda for the board within 3 or 6 months a process to start developing a climate transition roadmap to 2050 with transparent carbon neutrality or reduction targets, with clear interim targets to 2040, 2030, and within the current rolling multi-year strategic plan, and periodically thereafter report back to the board;
- c) delegate to the appropriate committee(s) of the board, such as risk, audit, legal and governance, scenarios/strategy, nominations/remuneration, or sustainability/corporate responsibility, the task of translating the long-term strategy into a clear decision-making process for each aspect that is relevant to each committee; and
- d) discuss with disclosure counsel, to develop an external engagement and communications plan and to oversee rigorous disclosure and accounting.

Contributors: Dr. Ernest Lim, Associate Professor of Law, National University of Singapore
CCLI



EW Barker Centre for Law & Business
Faculty of Law



COMMONWEALTH
Climate and Law Initiative

²⁶⁸ Jeffrey Chan SC et al, 'Legal Opinion on Directors' Responsibilities and Climate Change Under Singaporean Law' (April 2021) at [69].

South Africa

The South African Reserve Bank, Prudential Authority and Financial Sector Conduct Authority each recognize that climate change poses systemic risks to the financial system. In 2019, the Prudential Authority surveyed the South African banking and insurance sector's implementation of the Task Force on Climate-related Financial Disclosures' (TCFD) recommendations. As a result, the Prudential Authority intends to enhance its supervision of climate-related financial risks and to publish guidelines "outlining proposals to insurers and banks to consider climate risks".²⁶⁹

In May 2020, South Africa's financial regulators worked with the National Treasury to produce a technical paper entitled 'Financing a Sustainable Economy'.²⁷⁰ Moreover, in June 2020 the South African Reserve Bank, a member of the Network of Central Banks and Supervisors for Greening the Financial System, published a working paper entitled 'Climate Change and its Implications for Central Banks in Emerging and Developing Economies'.²⁷¹ This regulatory focus upon addressing climate-related financial risks also led to the establishment of the Prudential Authority Climate Think Tank (PACTT) in September 2020.²⁷² The PACTT's mandate is to promote, develop and coordinate the Prudential Authority's regulatory and supervisory response to climate risks.

Directors Duties and Climate Change

The fiduciary duties of South African directors that have been partially codified in the *Companies Act 71 of 2008* (Companies Act), are mandatory, and apply to all companies. The general duties of directors fall into two categories: fiduciary duties of good faith, honesty and loyalty; and the duty to exercise reasonable care, skill and diligence, which is not a fiduciary duty and instead centres on the issue of competence.

A 2018 report by the Commonwealth Climate and Law Initiative concluded that "fiduciary and other company law duties requiring company directors to act in the best interests of the company are likely to apply in the climate-risk context, given the material financial risks that climate change poses, which

²⁶⁹ Prudential Authority, 'Prudential Authority Annual Report 2019/2020' (2020), 13
<<https://www.resbank.co.za/en/home/publications/publication-detail-pages/reports/pa-annual-reports/2020/10227>>.

²⁷⁰ South African National Treasury, 'Financing a Sustainable Economy: Technical Paper 2020' (2020) <[http://sustainablefinanceinitiative.org.za/wp-content/downloads/Sustainability technical paper 2020.pdf](http://sustainablefinanceinitiative.org.za/wp-content/downloads/Sustainability%20technical%20paper%202020.pdf)>.

²⁷¹ South African Reserve Bank, 'Climate Change and its Implications for Central Banks in Emerging and Developing Economies', *Working Paper Series WP/20/04* (2020)
<<https://www.resbank.co.za/en/home/publications/publication-detail-pages/working-papers/2020/10001>>.

²⁷² Sustainable Insurance Forum, 'Jurisdiction: South Africa: Prudential Authority (PA)' (2020)
<https://www.sustainableinsuranceforum.org/view_pdf.php?pdf_file=wp-content/uploads/2020/11/South-Africa-Prudential-Authority-PA-1.pdf>.

are foreseeable, requiring company directors to develop strategies to manage these risks".²⁷³ These duties evolve with the values of society and what is considered to be the industry norm, or 'best practice', at any given time. In the South African context, the King Report, and the Constitution and Bill of Rights, are of particular relevance to the framing of climate issues within directors' duties.

On the issue of investor fiduciary duties and climate change, a leading South African pension lawyer, Rosemary Hunter of law firm Fasken, published an opinion in April 2019 that found that the boards of South African pension and provident funds are required, per their fiduciary duties, to fully consider climate risk when making investment decisions (the [Fasken opinion](#)).²⁷⁴ Failure to do so exposes trustees to the threat of legal liability for losses incurred by the fund as a result.

Directors' Disclosure Obligations and Climate Change

According to the 2016 King IV Report on Corporate Governance (King IV),²⁷⁵ boards are advised that, in preparing their integrated report, they must address "matters that could significantly affect the organisation's ability to create value". King IV explicitly links value creation to the six capitals, one of which is natural capital. Entities listed on the Johannesburg Stock Exchange must report on their compliance with King IV's disclosure and application regime as part of their annual report.²⁷⁶ Non-listed entities are also encouraged to comply.

Disclosure in accordance with the TCFD's recommendations is also becoming a norm in South Africa. In a survey conducted by the Prudential Authority, 67% of banks and 100% of non-life insurers stated they intended to make TCFD-aligned disclosures in financial year 2019-2020.²⁷⁷ Furthermore, in November 2020 the Code for Responsible Investing in South Africa (CRISA) Committee released their draft revised Code.²⁷⁸ The Code calls upon institutional investors to integrate sustainable finance

²⁷³ Christine Reddell, Commonwealth Climate and Law Initiative, *Directors' Liability and Climate Risk*:

South Africa - Country Paper (April 2018) <<https://ccli.ouce.ox.ac.uk/wp-content/uploads/2018/04/CCLI-South-Africa-Paper-Final.pdf>>.

²⁷⁴ Fasken, 'Pension Funds and Climate Risk' (April 2019) 2-3, 15-16 <https://justshare.org.za/wp-content/uploads/2019/04/2019_Pension-fund-legal-opinion-by-Fasken.pdf>

²⁷⁵ Institute of Directors in South Africa and King Committee on Corporate Governance, 'King Report on Corporate Governance for South Africa 2016' <https://cdn.ymaws.com/www.iodsa.co.za/resource/collection/684B68A7-B768-465C-8214-E3A007F15A5A/iodsa_King_IV_Report_-_WebVersion.pdf>

²⁷⁶ See *JSE Listings Requirements Service Issue 27*, [8.63(a)].

²⁷⁷ South African Prudential Authority, 'Survey Results: Task Force on Climate-related Financial Disclosures' (2020) *Prudential Authority Website* <<https://www.resbank.co.za/en/home/publications/publication-detail-pages/prudential-authority/public-awareness/Covid-19-Response/9855>>.

²⁷⁸ CRISA Committee, 'CRISA Code for Responsible Investment in South Africa: 2020 Revision Consultation Draft' (2020) <<https://collaborate.unpri.org/group/5346/stream>>.

practices (including climate resilience activities) into their operations and to disclose how such practices are being integrated, which standards, guidelines or models are being used and the outcomes of such implementation.

Practical Implications for Directors

Given that regulators in South Africa have become increasingly emphatic regarding the need for companies and their directors to adopt climate resilience measures in business practices and disclosure, and in particular the above-noted recognition of climate risk by the Reserve Bank Prudential Authority and Financial Sector Conduct Authority, the Government's coordination of sustainable finance analysis, the Faskin opinion on pension funds' climate change obligations, and King IV Report on Corporate Governance, well-counselled boards will:

- a) delegate climate risk identification and evaluation to a clearly-identified team in management which reports directly to the CEO and board;
- b) put on the agenda for the board within 3 or 6 months a process to start developing a climate transition roadmap to 2050 with transparent carbon neutrality or reduction targets, with clear interim targets to 2040, 2030, and within the current rolling multi-year strategic plan, and periodically thereafter report back to the board;
- c) delegate to the appropriate committee(s) of the board, such as risk, audit, legal and governance, scenarios/strategy, nominations/remuneration, or sustainability/corporate responsibility, the task of translating the long-term strategy into a clear decision-making process for each aspect that is relevant to each committee; and
- d) discuss with disclosure counsel, to develop an external engagement and communications plan and to oversee rigorous disclosure and accounting.

Contributors: CCLI



Switzerland

Sustainability, and environmental aspects in particular, are becoming increasingly important in Switzerland's legislation. In the past few years, there have been numerous legislative efforts aimed at reducing negative impacts on the climate and obliging companies to comply with certain due diligence and reporting obligations. On 29 November 2020, the Swiss electorate voted narrowly against the so-called Responsible Business Initiative, which would have opened up Swiss companies to litigation in Swiss courts for alleged violations of human rights or environmental laws around the world. As a result, a counterproposal to this initiative that is viewed as "more moderate" and is modelled after the EU Non-Financial Reporting Directive (*Directive 2014/95*) will most likely come into force in the near future (cf. below section on directors' disclosure obligations).

Furthermore, in September 2020, the Swiss Parliament adopted a revision of the current *Federal Act on the Reduction of CO₂ Emissions* (CO₂ Act), which was narrowly rejected by the Swiss electorate in June 2021.

On 10 November 2020, FINMA opened a consultation regarding an amendment to its Circulars 2016/1 "Disclosure – banks" and 2016/2 "Disclosure – insurers". Under existing regulations, banks and insurance companies are already required to provide adequate information to the public about their risks. These also include the consequences of climate change, which could pose significant financial risks for financial institutions in the longer term. FINMA now intends to specify the disclosure requirements pertaining to climate-related financial risks for systemically-important banks and large insurance companies. In terms of content, the disclosure requirements are based on the recommendations of the [Task Force on Climate-related Financial Disclosures](#) (TCFD).²⁷⁹

On 12 January 2021, the Swiss Federal Council officially pledged to support the TCFD, and as such, called on Swiss companies from all sectors of the economy to implement the recommendations of the TCFD on a voluntary basis. The Federal Council also announced that it intends to draft a bill to make the recommendations binding.²⁸⁰

²⁷⁹ Finma, 'Transparency obligations for climate risks – FINMA opens consultation' (November 2020) <<https://www.finma.ch/en/news/2020/11/20201110-mm-transparenzpflichten-klimarisiken/>>.

²⁸⁰ Finma, 'Switzerland promotes transparency on climate-related financial risks' (12 January 2021) <https://www.efd.admin.ch/efd/en/home/das-efd/nsb-news_list.msg-id-81924.html>.

Directors' Duties and Climate Change

The duties of the directors of Swiss companies are primarily governed by the *Swiss Code of Obligations* (CO). The legal provisions are supplemented by soft law, such as the Swiss Code of Best Practice.²⁸¹

According to article 716a CO, the board of directors is *inter alia* responsible for the overall management of the company, the determination of the company's organisation, the organisation of the accounting, financial control and financial planning systems and the overall supervision of the persons entrusted with managing the company. In particular, the board of directors must define the company's strategy and ensure that the strategy is in the company's best interests and can be implemented with the resources available. The board of directors also needs to ensure that the company's risks are sufficiently identified, assessed and managed.

The members of the board of directors and third parties engaged in managing the company's business must perform their duties with all due diligence and safeguard the interest of the company in good faith (article 717 CO). If the directors intentionally or negligently breach their duties, they are liable both to the company and to the individual shareholders and creditors for any losses or damage arising from the breach of their duties (article 754 CO).

The law does not explicitly stipulate that directors must also take climate-related risks into account when determining the company's strategy and overseeing its risk management systems. However, in light of the developments mentioned above, in particular the widespread recognition by financial regulators that climate change poses material financial risks to business and the new ESG reporting requirements, it logically follows that directors must integrate climate risks and opportunities into their governance roles.

Directors' Disclosure Obligations and Climate Change

As explained at the outset, the so-called Responsible Business Initiative was rejected in November 2020. However, as a counter-proposal to this initiative, the Swiss Parliament introduced new ESG reporting and due diligence requirements. This new law may still be challenged by collecting 50,000 signatures within 100 days after official publication of the new law in the Swiss Federal Gazette, which is still pending (so-called optional referendum). In this, rather unlikely, case, the Swiss electorate would vote on the adoption of the law. If no such referendum is requested, the new reporting and due diligence requirements will take effect for the first time in

²⁸¹ *economiesuisse*, 'Swiss code of best practice for corporate governance' (2016) <https://www.economiesuisse.ch/sites/default/files/publications/economiesuisse_swisscode_e_web_2.pdf>.

the financial year commencing one year after the new provisions come into force. We therefore expect that affected companies will have to apply the new requirements in the 2023 financial year.

The ESG reporting obligation will apply to companies of public interest (i.e., listed companies, banks, insurance companies and other supervised financial institutions) that are domiciled in Switzerland, and that, together with controlled companies in Switzerland and abroad, (i) have at least 500 FTEs on annual average, and (ii) exceed assets of CHF 20 million or revenues of CHF 40 million in two consecutive years. Companies that are controlled by a company to which the new reporting requirements apply, or that are subject to equivalent reporting under foreign laws, are not required to prepare an additional report.

The ESG report must include information necessary to understand the company's business and the impact of its activities on the environment (including CO₂ targets), as well as societal concerns related to employees, respect for human rights and the fight against corruption across their value chains.²⁸²

As indicated at the outset, the ESG reporting requirement is modelled after the EU Non-Financial Reporting Directive (*Directive 2014/95*), and the non-exhaustive list of topics that the report must cover tracks its model closely. Specifically, the report has to cover the following topics:

- the company's business model (Business Model);
- the main ESG risks resulting from the company's own operations and, where relevant and proportionate, its business relationships, products or services (Risk Assessment);
- the policies pursued to address these ESG risks, including due diligence applied (Policies and Due Diligence);
- the outcome of these policies (Outcome); and
- non-financial key performance indicators related to the company's response to ESG risks (KPIs).

If a company does not have policies addressing certain ESG risk areas, the report must include an explanation of the reasons for such a gap ("comply or explain"). The only defensible explanation that one could expect to see is an assessment that a company's activities do not raise concerns in a certain area.

²⁸² In addition to the generic ESG reporting obligation, the new ESG legislation provides for further specific due diligence and reporting obligations related to so-called Conflict Minerals and related to child labour.

The report may be based on national, European or international reporting standards, such as for example the [OECD Guidelines for Multinational Enterprises](#)²⁸³ or the standards of the [Global Reporting Initiative \(GRI\)](#).²⁸⁴ Further, companies may want to draw from guidelines the EU has issued on the methodology for reporting non-financial information.²⁸⁵ Under the above headings, these guidelines list out in detail the aspects that the ESG report should cover.

The report may be established in one of the Swiss national languages (i.e., German, French or Italian), or in English. It must be approved by the board of directors and the shareholders' meeting and made electronically accessible to the public during a period of 10 years. However, unlike the company's financial statements, there is no requirement for the ESG report to be audited.

Non-compliance with the new ESG reporting regime is subject to criminal liability. Non-compliance includes the inclusion of false statements in any of the newly-required reports, the generic ESG Report and the report on compliance with due diligence measures in the area of conflict minerals and child labour, or the failure to issue any of these reports, or the failure to keep records of, or publish, these reports. If any of these acts is committed intentionally, the fine is up to CHF 100,000; if committed negligently, the fine is up to CHF 50,000.

In addition, deficient ESG due diligence or reporting may trigger civil liability under existing law, namely the liability of board members and management under article 754 of the Swiss Code of Obligations.

Practical Implications for Directors

In addition to our standing recommendation to develop and maintain a well-documented and effective general Compliance Program, we suggest that in response to the developments laid out in this note, board directors lend particular attention to the following points as a matter of priority:

- a) Review and where required adjust governance to ensure appropriate leadership at the board level in relation to climate-related risks, including adverse impacts the company's activities may cause and legal risks the company may face;

²⁸³ OECD, OECD Guidelines for Multinational Enterprises (2011) <<http://www.oecd.org/daf/inv/mne/48004323.pdf>>.

²⁸⁴ GRI, GRI Standards (May 2020), accessible at: <<https://www.globalreporting.org/how-to-use-the-gri-standards/gri-standards-english-language/>>.

²⁸⁵ European Commission Communication, 'Guidelines on Non-financial Reporting: Supplement on Reporting Climate-related Information', 2019/C 209/1, (20 June 2019) <https://ec.europa.eu/finance/docs/policy/190618-climate-related-information-reporting-guidelines_en.pdf>.

- b) Designate responsible function(s) to monitor and provide ongoing advice in relation to the increasing body of laws and regulations in the area of climate risk management requirements both in Switzerland and in their companies' markets abroad;
- c) Delegate climate risk identification and evaluation to a clearly-identified team in management that reports directly to the CEO and board, and is charged with bringing together all key functions, including the Legal and/or Compliance function, Enterprise Risk Management, Strategic Planning, Audit, Remuneration, Human Resources, Investor Relations, Stakeholder Relations, etc.;
- d) Review and where required adjust climate-related risk management policies and processes across the company's supply chain and distribution network, including affiliates and third parties, on the basis of a solid risk assessment. In this regard, broaden and deepen the company's third party intermediary due diligence framework to address climate-related risk factors and do so into tiers 2 and 3 of their companies' supply chains;
- e) Review and where required adjust their reporting on climate-related risk factors and the measures they take to address these risks. Introduce internal assurance processes in relation to reporting; and
- f) Given ongoing disruption by Covid-19, review and where required adjust the design of their companies' Compliance Programs to allow for increased remote execution while still ensuring required effectiveness and documentation standards. This may require an increased level of central data collection along pre-defined risk factors instead of onsite reviews.

Contributors: Philippe Reich, Baker McKenzie Switzerland
Corinne Nacht, Baker McKenzie Switzerland



United Kingdom

The Bank of England, the Financial Conduct Authority (FCA), the Financial Reporting Council (FRC), and the Pensions Regulator released a joint statement in 2019 setting out their position on climate change.

Climate change is one of the defining issues of our time. We recognise it presents far-reaching financial risks relevant to our mandates from both physical factors, such as extreme weather events, and transition risks that can arise from the process of adjustment to a carbon-neutral economy. Companies should consider the likely consequence of climate change on their business decisions, in addition to meeting their responsibility to consider the company's impact on the environment.²⁸⁶

Directors' Duties and Climate Change

Historically, company directors owed duties to their company under common law. However, in 2006, directors' duties were codified in the *Companies Act 2006*.²⁸⁷ Two relevant duties are the duty to promote the success of the company for the benefit of its members as a whole (section 172), and the duty to exercise reasonable care, skill, and diligence (section 174), the latter of which is not fiduciary in nature.²⁸⁸ The duty to promote the success of the company has been described as the 'principal duty',²⁸⁹ consistent with the primacy of the duty of loyalty at common law.²⁹⁰ Section 174 further informs the exercise of section 172 by directors by setting standards for the manner in which directors are expected to act and the knowledge, skill and experience they should hold.

Given the breadth and potential materiality of climate change-related risks, it seems increasingly likely that directors should consider these when fulfilling their duty under section 172.²⁹¹ Discussing this in August 2019, Lord Sales, Justice of the U.K. Supreme Court, delivered a speech on

²⁸⁶ Joint statement on climate change by the Bank of England, Financial Conduct Authority, Financial Reporting Council and the Pensions Regulator (2 July 2019) <<https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/publication/2019/joint-statement-on-climate-change.pdf>>.

²⁸⁷ See generally *Companies Act 2006* (UK) sections 171-177.

²⁸⁸ *Maidment v Attwood & Ors* [2012] EWCA Civ 998, [22].

²⁸⁹ See Rosemary Teele Langford, 'The Duty of Directors to Act Bona Fide in the Interests of the Company: A Positive Fiduciary Duty? Australia and the UK Compared' 11(1) *Journal of Corporate Law Studies* (2011) 215, 234.

²⁹⁰ *Bristol and West Building Society v Mothew* [1998] Ch 1, 16 (Millet LJ): the 'obligation of loyalty' is the distinguishing, 'core' obligation of a fiduciary.

²⁹¹ See Alexia Staker and Alice Garton, Commonwealth Climate and Law Initiative, *Directors' Liability and Climate Risk: United Kingdom - Country Paper* (April 2018) <<https://ccli.ouce.ox.ac.uk/wp-content/uploads/2018/04/CCLI-UK-Paper-Final.pdf>>.

directors' duties in respect of climate change.²⁹² Lord Sales recognised the links between directors' duties and climate change, noting that general fiduciary and duty of care obligations may require directors to have regard to climate-related risks and to take action to reduce their contribution to climate change.

Additionally, in promoting the success of the company under section 172, directors are required to "have regard" to a non-exhaustive list of factors. This includes "the impact of the company's operations on the community and environment" (section 172(1)(d)) which captures consideration of climate change issues.

Therefore, when fulfilling their duty to promote the success of their company, directors should consider climate change risks both in light of the general duty under section 172 and the requirement to have regard to climate change issues. A well-counselled director should ensure that they consider climate-related issues in good faith as they carry out their role, using their own skill and judgment, and having regard to the likely long-term consequences of the decision being considered.

In addition to directors' duties, regulators in the U.K. are increasingly focusing on climate-related issues. The Bank of England Prudential Regulation Authority now requires banks to manage climate risk and to integrate it into their risk management frameworks.²⁹³ The PRA amplified this with a July 2020 'Dear CEO' letter expressing its view that banks and insurers were not moving fast enough in their efforts to manage climate-related financial risks, and clarifying that regulated firms have until the end of 2021 before the introduction of a supervisory ratchet.²⁹⁴ The PRA's stress tests for major banks and insurers will for the first time include climate risks in 2021.

Directors' Disclosure Obligations and Climate Change

Climate-related disclosures may need to be integrated into various sections of corporate reporting on which directors need to sign off, including Strategic Reports, the section 172 statement, and the financial statements.

²⁹² Lord Sales, Directors' duties and climate change: keeping pace with environmental challenges,' (27 August 2019) <<https://www.supremecourt.uk/docs/speech-190827.pdf>>

²⁹³ Bank of England PRA, *Supervisory Statement 3/19: Enhancing banks' and insurers' approaches to managing the financial risks from climate change* (April 2019) <<https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/supervisory-statement/2019/ss319>>; see also <https://www.bankofengland.co.uk/news/2020/June/the-cfrf-publishes-guide-to-help-financial-industry-address-climate-related-financial-risks>.

²⁹⁴ PRA, Letter from Sam Woods 'Managing climate-related financial risk – thematic feedback from the PRA's review of firms' SS3/19 plans and clarifications of expectations' (1 July 2020) <<https://www.bankofengland.co.uk/prudential-regulation/letter/2020/managing-the-financial-risks-from-climate-change>>.

The Strategic Report must include information about environmental matters, including the impact of the company's business on the environment, with additional disclosures in this regard being required following implementation of the EU Non-Financial Reporting Directive in the U.K. The Strategic Report must also include a section 172 statement on how the board has complied with its duty to promote the success of the company, including by having regard to the impacts of the company on the environment.

The FRC published guidance in July 2018 on companies' annual Strategic Reports, advising companies to report on climate-related risk where "material".²⁹⁵ In October 2019, the Financial Reporting Lab (Lab) published guidance on how companies can better meet growing investor expectations of effective reporting on climate-related risks by using the Task Force on Climate-related Financial Disclosures (TCFD) recommendations as a guiding framework.²⁹⁶ The U.K. Government's Green Finance Strategy in July 2019 sets out its expectation that large asset owners and listed companies should disclose in line with the TCFD recommendations by 2022.²⁹⁷ The FRC published a thematic review on climate change reporting in November 2020 which identified that improvements were required. It supported the introduction of global standards on non-financial reporting, but, as an interim step, encouraged public interest entities to report against the TCFD's recommended disclosures and the Sustainability Accounting Standards Board metrics for their sector.

In November 2020, the U.K. Chancellor of the Exchequer announced that TCFD-aligned disclosure will be mandatory "across the economy" as of 2025, and will be required from "listed commercial companies, U.K.-registered large private companies, banks, building societies, insurance companies, U.K.-authorised asset managers, life insurers, FCA-regulated pension schemes, and occupational pension schemes."²⁹⁸ In March 2021, the Department for Business, Energy and Industrial Strategy launched a consultation on this proposed requirement, including a proposal that climate change-related financial information should be included in the Strategic Report.²⁹⁹

²⁹⁵ Financial Reporting Council Guidance on the Strategic Report (July 2018): 44-45 <<https://www.frc.org.uk/getattachment/fb05dd7b-c76c-424e-9daf-4293c9fa2d6a/Guidance-on-the-Strategic-Report-31-7-18.pdf>>. See also Janis Sarra, "Following the Footpath to Mandatory TCFD Disclosure in the United Kingdom: Lessons for Canadian and Other Regulators", (forthcoming June 2021, Canada Climate Law Initiative (ubc.ca)).

²⁹⁶ Financial Reporting Lab, 'Climate-related corporate reporting: where to next?' (October 2019) <<https://www.frc.org.uk/getattachment/22ee8a43-e8ca-47be-944b-c394ecb3c5dd/Climate-Change-v9.pdf>>.

²⁹⁷ HM Treasury and Department for Business, Energy & Industrial Strategy, Green Finance Strategy (July 2019) <<https://www.gov.uk/government/publications/green-finance-strategy>>.

²⁹⁸ HM Treasury, *Chancellor sets out ambition for future of UK Financial Services*, (9 November 2020) <<https://www.gov.uk/government/news/chancellor-sets-out-ambition-for-future-of-uk-financial-services>>.

²⁹⁹ HM Government and Department for Business, Energy & Industrial Strategy, *Consultation on requiring mandatory climate-related financial disclosures by publicly quoted companies, large private companies and Limited Liability Partnerships (LLPs)* (March 2021) <https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/972422/Consultation_on_BEIS_mandatory_climate-related_disclosure_requirements.pdf>.

Reporting against the TCFD's recommended disclosures is already mandatory for premium-listed companies in the U.K. In December 2020, the FCA implemented amendments to the listing rules in December 2020 to implement TCFD disclosure reporting for premium-listed companies on the London Stock Exchange (other than investment companies) on a comply or explain basis for financial years starting on or after 1 January 2021.³⁰⁰ The FCA intends to broaden the scope of this requirement between 2021-2025 to cover a wider range of FCA-regulated companies.³⁰¹ These disclosures are more extensive than those proposed by BEIS to apply to the wider range of companies,³⁰² but are on a comply or explain basis rather than being fully mandatory. The FCA is also sharing views and expertise internationally through its co-chairing a workstream on disclosure as part of IOSCO's Sustainable Finance Task Force.³⁰³

Practical Implications for Directors

Given that regulators in the U.K. have become increasingly emphatic regarding the need for companies and their directors to adopt climate resilience measures in business practices and disclosures (in particular the above-noted recognition of climate risk by the Bank of England, the FCA, the FRC and the Pensions Regulator), and the coming into effect of required TCFD disclosure, well-counselled boards will:

- a) delegate climate risk identification and evaluation to a clearly-identified team in management which reports directly to the CEO and board;
- b) put on the agenda for the board within 3 or 6 months a process to start developing a climate transition roadmap to 2050 with transparent carbon neutrality or reduction targets, with clear interim targets to 2040, 2030, and within the current rolling multi-year strategic plan, and periodically thereafter report back to the board;
- c) delegate to the appropriate committee(s) of the board, such as risk, audit, legal and governance, scenarios/strategy, nominations/remuneration, or sustainability/corporate responsibility,

³⁰⁰ FCA, *PS20/17: Proposals to enhance climate-related disclosures by listed issuers and clarification of existing disclosure obligations* (December 2020)
<<https://www.fca.org.uk/publication/policy/ps20-17.pdf>>.

³⁰¹ FCA, HM Treasury, Department for Business, Energy & Industrial Strategy, Department for Work and Pensions, The Pensions Regulator. *A Roadmap towards mandatory climate-related disclosures* (November 2020)
<https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/933783/FINAL_TCFD_ROADMAP.pdf>.

³⁰² The proposed disclosures require reporting in line with the four 'pillars' of the TCFD recommendations (Governance, Strategy, Risk Management and Metrics and Targets), rather than requiring disclosures in line with the 11 specific TCFD recommendations within these categories, which are required by the listing rules.

³⁰³ *Ibid.*

the task of translating the long-term strategy into a clear decision-making process for each aspect that is relevant to each committee; and

- d) discuss with disclosure counsel, to develop an external engagement and communications plan and to oversee rigorous disclosure and accounting.

Contributors: Alex Cooper, CCLI



COMMONWEALTH
Climate and Law Initiative



**Chapter
Zero**
The UK Directors' Climate Forum

United States

President Biden has moved quickly to emphasize climate change as part of both U.S. foreign and domestic policy. On his first day of office, 20 January 2021, he declared support for the Paris Climate Agreement and its threefold goals of “a safe global temperature, increased climate resilience, and financial flows aligned with a pathway toward low greenhouse gas emissions and climate-resilient development.”³⁰⁴ His climate change Executive Order on 27 January 2021 established a process to embed climate risk mitigation in every executive agency of the federal government, including establishing an inter-agency coordinating process and appointing both a foreign and domestic policy lead in newly-established positions within the White House.³⁰⁵ Even more ambitiously, on 31 March 2021, the Biden Administration announced a Jobs Plan for infrastructure reform that also addresses the climate crisis.³⁰⁶

Secretary of the Treasury Janet Yellen has stated that climate change will be a priority, creating a hub within Treasury that will focus on financial system-related risk posed by climate change, and tax policy incentives to effect change.³⁰⁷ In a speech 21 April 2021, she vowed to build on President Biden’s “whole of government” approach with a “whole of economy” approach.³⁰⁸ One month later, President Biden issued an Executive Order on Climate Change Financial Risk, with responsibilities for Treasury, the Office of Management and Budget (OMB), and the Financial Stability Oversight Council (FSOC) and its constituent agencies.³⁰⁹ Among its significant aspects are initiatives to:

- (1) require the development of a government-wide strategy to assess, measure, mitigate, and disclose climate change financial risk across the Federal Government;
- (2) request a financial analysis of the capital needed to move the American economy to net-zero by 2050;

³⁰⁴ The White House, ‘Paris Climate Agreement: Acceptance on Behalf of the United States of America’ (20 January 2021) <<https://www.whitehouse.gov/briefing-room/statements-releases/2021/01/20/paris-climate-agreement/>>.

³⁰⁵ The White House, *Executive Order on Tackling the Climate Crisis at Home and Abroad*, (27 January 2021), <<https://www.whitehouse.gov/briefing-room/presidential-actions/2021/01/27/executive-order-on-tackling-the-climate-crisis-at-home-and-abroad>>.

³⁰⁶ The White House, ‘Fact Sheet: The American Jobs Plan’ (31 March 2021) <<https://www.whitehouse.gov/briefing-room/statements-releases/2021/03/31/fact-sheet-the-american-jobs-plan/>>.

³⁰⁷ Reuters, ‘Yellen says would appoint senior climate official at Treasury’ (19 January 2021), <<https://www.reuters.com/article/us-usa-biden-yellen-climate-idUSKBN29O2B3>>.

³⁰⁸ U.S. Department of the Treasury, ‘Secretary of the Treasury Janet L. Yellen’s Remarks to the Institute of International Finance’ (21 April 2021) <<https://home.treasury.gov/news/press-releases/jy0139>>.

³⁰⁹ The White House, *Executive Order on Climate Related Financial Risk* (20 May 2021) <<https://www.whitehouse.gov/briefing-room/presidential-actions/2021/05/20/executive-order-on-climate-related-financial-risk/>>.

- (3) require Treasury to work with FSOC and its constituent agencies to identify actions within each agency to identify, measure, mitigate, and disclose climate change financial risk;
- (4) identify financial risk from climate within the insurance industry;
- (5) identify actions that can be taken by the Department of Labor to protect pension savings and Federal pension insurance from climate change financial risk; and
- (6) identify how the Federal Government can incorporate climate change financial risk into its lending, risk underwriting, procurement, and budgeting.³¹⁰

These actions are consistent with conclusions by the Federal Reserve Bank Board of Governors, which for the first time identified climate change as a risk to the American financial system in its Financial Stability Report (Report) of November 2020.³¹¹ The Report stated that further analysis would be required, since:

Climate change adds a layer of economic uncertainty and risk that we have only begun to incorporate into our analysis of financial stability. Different sectors of the economy and geographic regions face different risks that will diverge from historical patterns [...] [C]limate change, which increases the likelihood of dislocations and disruptions in the economy, is likely to increase financial shocks and financial system vulnerabilities that could further amplify these shocks.³¹²

As part of its Report, the Federal Reserve stated that “Federal Reserve supervisors expect banks to have systems in place that appropriately identify, measure, control, and monitor all of their material risks, which for many banks are likely to extend to climate risks.”³¹³

A subcommittee of the U.S. Commodity Futures Trading Commission has likewise recognised the “serious emerging risks” to the U.S. financial system posed by climate change and has urged U.S. financial regulators to “move urgently and decisively to measure, understand, and address these risks”.³¹⁴

³¹⁰ *Ibid.*

³¹¹ United States Federal Reserve Bank Board of Governors, *Financial Stability Report*, 59-60 (November 2020).

³¹² *Ibid.* at 59.

³¹³ *Ibid.*

³¹⁴ Climate-Related Market Risk Subcommittee, Market Risk Advisory Committee of the U.S. Commodity Futures Trading Commission, ‘Managing Climate Risk in the U.S. Financial System: Report of the Climate-Related Market Risk Subcommittee, Market Rise Advisory Committee of the U.S. Commodity Futures Trading Commission,’ (September 2020) ii <<https://www.cftc.gov/sites/default/files/2020-09/9-9-20%20Report%20of%20the%20Subcommittee%20on%20Climate->

Directors' Duties and Climate Change

Directors' fiduciary duties are sourced in state corporate legislation and the common law, as developed by the courts. A majority of U.S. public companies are incorporated in the state of Delaware. Directors' core fiduciary duties are the duty of loyalty, which includes a duty to act in good faith without conflicts of interests, and in the best interest of the company; and the duty of care, which means making decisions on an informed basis after reasonable inquiry and deliberation. The duty of loyalty also includes a duty to provide adequate oversight of legal compliance, including by ensuring that reasonable information and reporting systems are implemented and maintained to provide the board and senior management with timely, accurate information to support informed decision-making. This ancillary duty is often called the board's *Caremark* duty based on the case that established it.³¹⁵

Caremark duties have recently been given new emphasis when, in 2019, the Delaware Supreme Court allowed a duty of oversight claim to go forward in *Marchand v. Barnhill*,³¹⁶ giving guidance on directors' responsibilities for oversight of "mission critical" operations and compliance risk. In *Marchand*, a case involving the Blue Bell ice cream manufacturer, the Court allowed the case to go forward because the plaintiff had provided enough facts to potentially prove a "dearth of any board-level effort at monitoring" to ensure board oversight of health, safety, and sanitation controls.³¹⁷ *Marchand* may signal a doctrinal development in oversight liability that both expands the scope of the doctrine to operational oversight over "mission critical" aspects of the business, and expresses higher expectations of board vigilance regarding such core operations. This conclusion is consistent with three other recent oversight decisions applying *Marchand* to allow cases to proceed.³¹⁸ These cases might provide scope for fiduciary liability if a board has not ever turned its collective attention to analysing the relevance of

[Related%20Market%20Risk%20-%20Managing%20Climate%20Risk%20in%20the%20U.S.%20Financial%20System%20for%20posting.pdf>](#)

³¹⁵ *In re: Caremark Int'l Derivative Litigation*, 698 A.2d 959 (Ch.Ct.Del.1996). *Caremark* construed the duty of oversight as part of the board's duty of care, but a later Delaware Supreme Court opinion reconceptualized it as an aspect of the duty of loyalty, not care. See *Stone v. Ritter*, 911 A.2d 362 (Del.2006).

³¹⁶ *Marchand v Barnhill*, 212 A.3d 805 (Del.2019). The board had exercised no oversight of operations or food safety in the company's ice cream plants, leading to a *listeria* outbreak in which three people died, and the company's entire inventory had to be recalled and destroyed. These facts were sufficient to allege a breach of the board's duty of loyalty under *Caremark*. The parties agreed to a \$60 million settlement less than a week prior to the scheduled commencement of the trial: Longhurst, Jennifer and DiPonio, Joseph, 'Canada: Canadian Directors Should Heed Recent US Caremark Litigation', Mondaq Business Briefing, 18 June 2020.

³¹⁷ *Marchand v Barnhill*, 212 A.3d 805 (Del.2019).

³¹⁸ *In re Clovis Oncology Inc. Derivative Litigation*, C.A.No.2017-0222-JRS (2019) (failure of oversight of pharmaceutical company's research protocols); *Hughes v. Xiaoming Hu*, C.A.No.2019-0112-JTL (Apr.27, 2020) (failure of oversight over audited financial statements and internal accounting function); *Teamsters Local 443 Health Servs. v. Chou*, C.A.No.2019-0816-SG (Del.Ch.Aug.24, 2020)(failure of oversight over indirect subsidiary's criminal activities regarding handling of pharmaceutical injections).

climate change risks to the company, its operations, long-term strategy, or disclosure.

In exercising their fiduciary duties, directors are charged with maintaining a long-term focus. In a 2017 case involving a conflict between short-term and longer-term shareholder interests, the Delaware Chancery Court confirmed the “the fiduciary relationship requires that the directors act prudently, loyally, and in good faith to maximize the value of the corporation over the long-term...”³¹⁹ It added, “The fact that some holders of shares might be market participants who are eager to sell and would prefer a higher near-term market price likewise does not alter the presumptively long-term fiduciary focus.”

Directors' Disclosure Obligations and Climate Change

Public companies' disclosure obligations are governed by federal securities laws³²⁰ and regulations.³²¹ In 2010, the U.S. Securities and Exchange Commission (SEC) issued specific guidance to public companies to clarify their climate change-related disclosure obligations pursuant to risk factors disclosure requirements, management discussion and analysis (MD&A) requirements, and general materiality principles. The guidance emphasized that every company should consider how climate change impacts their operations and financial statements, including both direct and indirect impacts, such as impacts on suppliers and customers. It stated that:

Legal, technological, political, and scientific developments regarding climate change may create new opportunities or risks for registrants. These developments may create demand for new products or services, or decrease demand for existing products or services... These business trends or risks may be required to be disclosed as risk factors or in MD&A.³²²

The SEC identified regulatory and legislative developments at a state, federal, and transnational level that could increase or decrease prices as issues to be evaluated for disclosure, such as cap-and-trade arrangements among various states and countries; or new fuel standards. It also discussed physical changes from climate change as similarly requiring analysis, such as increased frequency and intensity of storms having

³¹⁹ *Frederick Hsu Living Trust v. ODN Holding Corp*[i]., No.12108-VCL, 2017 WL 1437308 (Del.Ch.Apr.24, 2017).

³²⁰ See generally *Securities Act of 1933 and Securities Exchange Act 1934* (for public disclosures).

³²¹ See generally *Regulation S-K, Standard Instructions for Filing Forms under Securities Act of 1933, Securities Exchange Act of 1934, and Energy Policy and Conservation Act of 1975*, 17 C.F.R. §§ 229.10-229.1016 (2020).

³²² Securities and Exchange Commission, *Commission Guidance Regarding Disclosure Related to Climate Change*, Release No.33-9106; 34-61469; FR-82 (8 February 2010).

financial implications for insurance companies, property firms, and mortgage lenders, for instance.³²³

The SEC is now widely expected to promulgate climate change and ESG disclosure requirements.³²⁴ Two of its five current Commissioners are on record in support of expanded climate change disclosure (Commissioners Lee and Crenshaw), and a new position, Senior Policy Advisor for Climate and ESG, has been created within the SEC.³²⁵ Chair Gary Gensler, confirmed on 14 April 2021, has inherited an agency that has begun a process to consider expanded climate and ESG disclosure. In early March 2021, the SEC announced an enforcement task force that will focus on problems with companies' climate and ESG disclosure.³²⁶ In mid-March, a pre-regulatory request for public comment on climate and ESG disclosure was published.³²⁷

Practical Implications for Directors

Given that regulators in the U.S. have become increasingly emphatic regarding the need for companies and their directors to adopt climate resilience measures in business practices and disclosure, and in particular the above-noted recognition of climate risk by the President, the Federal Reserve Bank Board of Governors, the U.S. Treasury, and the SEC; obligations for the Office of Management and Budget and the Financial Stability Oversight Council to incorporate climate risk into their work across the Federal Government; and the likely coming into effect of expanded climate and ESG disclosure across the economy, particularly for financial institutions, including insurance companies, well-counselled boards will:

- a) delegate climate risk identification and evaluation to a clearly identified team in management which reports directly to the CEO and board;
- b) put on the agenda for the board within 3 or 6 months a process to start developing a climate transition roadmap to 2050 with transparent carbon neutrality or reduction targets, with clear interim targets to 2040, 2030, and within the current rolling multi-year strategic plan, and periodically thereafter report back to the board;

³²³ *Ibid.*

³²⁴ See, e.g., Wachtell, Lipton, Rosen & Katz, 'ESG Disclosures: SEC Appoints Climate and ESG Policy Advisor; U.K. and EU Regulators Ramp Up Reporting Requirements', (4 February 2021) (discussing likely SEC actions to require expanded disclosure of climate and ESG matters).

³²⁵ *Ibid.* Satyam Khanna has been appointed to this position. Mr Khanna was previously counsel to former SEC Commissioner Robert Jackson, who was also on record as being in favor of expanded climate and ESG disclosure.

³²⁶ *Ibid.*, SEC, SEC Announces Enforcement Task Force Focussed on Climate and ESG Issues (4 March 2021) <<https://www.sec.gov/news/press-release/2021-42>>.

³²⁷ SEC, Public Input Welcome on Climate Change Disclosures (March 15, 2021)

<<https://www.sec.gov/news/public-statement/lee-climate-change-disclosures>>.

- c) delegate to the appropriate committee(s) of the board, such as risk, audit, legal and governance, scenarios/strategy, nominations/remuneration, or sustainability/corporate responsibility, the task of translating the long-term strategy into a clear decision-making process for each aspect that is relevant to each committee; and
- d) discuss with disclosure counsel, to develop an external engagement and communications plan and to oversee rigorous disclosure and accounting.

For Directors of Banks, Insurance Companies and Asset Managers

Given the special attention paid by the Treasury to the implications of climate risk for systemic financial stability, and the focus of FSOC on the insurance sector, well-counselled boards of companies in the banking, insurance, and fund management sectors will:

- a) Monitor closely the evolution of the [Network of Central Banks and Supervisors for Greening the Financial System \(NGFS\)](#), of which the [U.S. Federal Reserve became a member](#) in December 2020, as it develops specialized guidance for prudential regulators aimed at addressing climate-related systemic financial risk;
- b) Engage with their Chief Risk Officers to ensure the robustness of internal control systems to assess, mitigate, and monitor exposure to climate risk embedded in their portfolios of loans, insurance customers and investments, insofar as the exposure of these companies to climate risk may affect their credit quality, insurance risk profile, and market valuations;
- c) Incorporate climate climate-related scenario-modelling and stress-testing within their regular risk oversight responsibilities;
- d) Oversee innovation and product development opportunities related to expansion of the low-carbon economy; and
- e) Monitor the emergence of new disclosure criteria affecting the finance sector.

Contributors: Professor Cynthia Williams, York University, Canada Climate Law Initiative, CCLI

Ukraine

In 2018, Ukraine adopted the Low Emission Development Strategy 2050, which defines a potential pathway for economic development that takes due account of the goals set by state policy on emissions reduction and greenhouse gases emissions absorption. Implementation of this strategy will inevitably have a significant impact on the private sector. Therefore, substantial legislative and institutional developments envisaged by the strategy should be taken into account by company directors.

Directors' Duties and Climate Change

Ukrainian law³²⁸ imposes certain general duties on directors of companies. The fundamental duties of directors include, *inter alia*, the duty to act in the best interests of their company, to act diligently and in good faith, to act within their powers. A more detailed and comprehensive list of director's duties and authorities is set out in each company's charter.

Directors are liable for losses to their companies caused by their wilful misconduct or inaction. In such cases, the companies' founders (shareholders) may submit a derivative claim on behalf of the company.

Although the law does not explicitly provide for directors' duties to address the risk of the adverse impacts of climate change on the company, their failure to do so may lead to damage suffered by the company. In such cases, the court would decide if the damage has been caused to the company by the directors' wilful misconduct, and if the loss was therefore the directors' fault as a matter of law.

Directors' Disclosure Obligations and Climate Change

A. Climate change and environment

Directors are responsible for ensuring that their companies comply with all relevant statutory obligations, including environment-related disclosure. In Ukraine, environmental monitoring by the state is conducted by means of collecting and processing data on environmental matters as reported by companies. Such state statistical reporting is mandatory and covers, among others, air and water. The following discusses reporting obligations most relevant to climate change:

³²⁸ Law of Ukraine "On Limited Liability and Additional Liability Companies" dated 6 February 2018, № 2275-VIII.

Law of Ukraine "On Joint-Stock Companies" dated 17 September 2008, № 514-VI.
Civil Code of Ukraine dated 16 January 2003, № 435-IV.

i. Greenhouse gas emissions

On 1 January 2021, the Law of Ukraine "*On Principles of Monitoring, Reporting and Verification of Greenhouse Gas Emissions*" entered into force. The law is deemed to be a step towards Ukrainian integration with the EU in terms of compliance with the EU *acquis* on environmental protection.

Companies operating equipment or facilities that produce greenhouse gases are obliged to prepare plans for monitoring their GHG emissions and submit them to the Ministry of Environment and Natural Resources of Ukraine for approval. They have to prepare annual reports on GHG emissions for verification by independent experts. The verified reports must then be further approved by the Ministry of Environment and Natural Resources of Ukraine.

According to the Ukrainian Law "*On Commercial Activities with Ozone-Depleting Substances and Fluorinated Greenhouse Gases*", dated 12 December 2019, separate accounting and reporting must be made on imports, exports and use of the aforementioned substances and fluorinated greenhouse gases.

ii. Atmospheric air pollution

All companies operating stationary sources of air emissions must annually submit to the state statistical authorities a report on emissions of pollutants and greenhouse gases into the atmospheric air (according to form No.2-tp (air)).

The data on emissions of pollutants from mobile sources (industrial, agricultural and other machinery, automobile etc.) must be submitted separately.

B. Securities and stock exchange-related disclosures

Ukrainian companies issuing securities listed on the stock exchange are obliged to submit annual management reports containing both financial and non-financial information characterizing the company's status and the prospects of its development. The report must include, *inter alia*, a description of the risks and uncertainties faced by the company in its business activities. In that context, we assume that any climate risk-related information may be considered by the company's management as relevant and should be disclosed in the annual management report.

We anticipate further legal developments on climate change in Ukraine soon. As such, the next iteration of this chapter might be more informative.

Practical implications for Directors

Despite climate change attracting more attention from the Government, Ukrainian legislation does not explicitly include any regulations on specific climate resilience measures that companies must take to adapt to climate change and minimize related risks. However, as the risks related to climate change become more obvious each year, and damage resulting from climate change can be better anticipated and measured, the following best practices should be considered by companies and their boards:

- a) delegate climate risk identification and evaluation to a clearly-identified team in management that reports directly to the CEO and board;
- b) put on the agenda for the board within 3 or 6 months a process to initiate the development of a climate transition roadmap to 2050 with transparent carbon neutrality or reduction targets, with clear interim targets to 2040, 2030 and the current rolling multi-year strategic plan, and periodically thereafter report back to the board;
- c) delegate to the appropriate committee(s) of the board, such as risk, audit, legal and governance, scenarios/strategy, nominations/remuneration, or sustainability/corporate responsibility, the task of translating the long-term strategy into a clear decision-making process for each aspect that is relevant to each committee; and
- d) initiate discussions with relevant sector associations and NGOs about the risks anticipated for the business and possible mitigation opportunities.

We anticipate further legal developments on climate change in Ukraine soon. As such, the next iteration of this chapter might be more informative.

Contributors: Oleksandr Kurdydyk, DLA Piper Ukraine
Kateryna Soroka, DLA Piper Ukraine





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