

ENFORCEMENT OF ENVIRONMENTAL TARGETS THROUGH CONTRACTS & MARKET ENFORCEMENT

Aslı Arda, University of Copenhagen, Faculty of Law, CEPRI & SHOC
Copenhagen, 10 November 2022

KØBENHAVNS UNIVERSITET



Structure

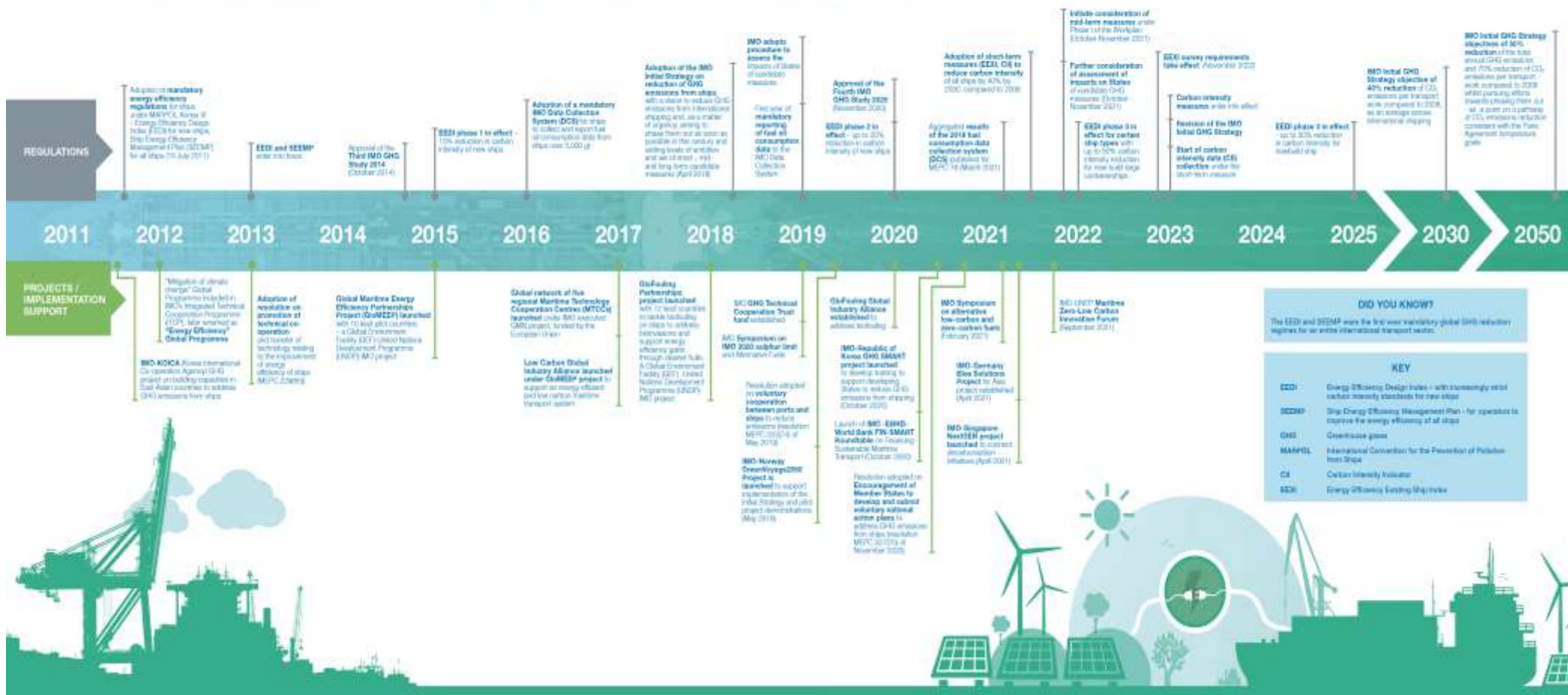
- Environmental Targets and Shipping Contracts
- Banks, Environmental Risks & Liability
- Enforcement of Environmental Targets





Addressing climate change

A decade of action to cut GHG emissions from shipping



Environmental Targets and Shipping Contracts

A wide variety of design, operational and economic solutions

Achieving the goals of the Initial IMO GHG Strategy will require a mix of technical, operational and innovative solutions applicable to ships. Some of them, along with indication on their approximate GHG reduction potential, are highlighted below.



<https://www.imo.org/en/MediaCentre/HotTopics/Pages/Cutting-GHG-emissions.aspx>

Charterparties

- Efficiency Existing Ship Index (EEXI), Carbon Intensity Indicator (CII)

Ship management contracts

- Ship Energy Efficiency Management Plan (SEEMP)

Ship Financing Agreements

- Data Collection System (DCS)
- Poseidon Principles
 - Looking through a 'green lens'
 - Measure & Report Carbon Emission
 - 30 signatories represent 65% of global ship loan
 - The power to fund decarbonization lies with finance organizations and this necessitates the evaluation of the position of the banks and environment, contractual impact of green financing and the issue of enforcement.

Banks and Environmental Risks

- Credit Risk
- Reputational Damage
- **Liability of lender**
 - The question of **climate change?**
 - US – Comprehensive Environmental Response, Compensation and Liability Act (**CERCLA**) 1980 – Superfund: current and former owners, operators for cleanup
 - Secured creditor exemption for the ones holding ownership as evidence of secured interest
 - *US v Fleet Factors Corporation* 901 F.2d 1550 (11th Cir. 1990) : widening the interpretation, 'ability to influence' (possibly ambiguous?)
 - OECD **NCP decisions** – Norwegian and Dutch Investors – 9 Oct 2012
 - Appropriate steps to be taken to prevent/mitigate the company's negative impacts on the environment
 - OECD Guidelines apply to all sectors including finance sector & to all investors regardless of being sub-group/minority shareholders

ENFORCEMENT OF ENVIRONMENTAL TARGETS THROUGH GREENSHIP FINANCE CONTRACTS & MARKET ENFORCEMENT



- What entities can do about enforcement?
- Poseidon Principles and the Standard Covenant Clause
- Environmental, Social and Governance (ESG) Clauses

Poseidon Principles Standard Covenant Clause (SCC)

- How the data pertaining to carbon emission of vessels is **disclosed**.
- Incorporation **not compulsory** but strongly recommended.
 - In practice, it is incorporated.
- Data disclosed is **confidential**
 - Unless consent given S/O or vessel is not identifiable in public. Detrimental effect?
- **Enforceability?** Not clear what remedies exist. Not all environmental covenants are enforceable & the element of conditionality may be added



<https://www.beano.com/posts/poseidon-facts>

Environmental, Social and Governance (ESG) Clauses and Market Enforcement

- The reflection of **ESG concerns of banks**. S/Os now developing relevant **strategy plans** to improve ESG performance so they **increase their chances to access financing** – making green attractive
- Various **ESG clauses** may be inserted
 - Reporting
 - Corrective Action Plan (CAP)
 - Climate remediation fees
- **Sustainability-linked financing** linked to the achievement of sustainability goals – improved financing/repercussions over interest rate
 - In January 2022 DNB Bank ASA got US\$154 million sustainability-linked secured term loan for fleet of ten vessels – margin ratchet pertaining to the achievement of Poseidon
 - The Chancery Lane Project – Noah's clause governs sustainability-linked lending
- A possible future question: can banks as private actors enforce EEXI and CII through their contract and make it conditional to conduct purchases in compliance with these?



TAK!

Source:
<https://www.nytimes.com/2021/08/17/arts/design/little-mermaid-denmark-dispute.html>

