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MANAGING NET ZERO OPPORTUNITIES AND RISK - SANTOS "CLEAN FUEL" AND THE CANARY

Key messages:

- The role of carbon capture and storage and blue hydrogen in the energy transition (and achieving net zero) is being questioned.
- Net zero plans with undisclosed qualifications and assumptions are dangerous. As are net zero plans that do not consider the broader context of business operations.
- Any net zero or environmental statements need to be reasonable and defensible at the time the statement is made.
- While not a new concern, beware of greenwashing, paying particular attention to "green" and "clean".
- The right balance is challenging to achieve, particularly in the context of evolving (and unproven) complex technology, customer and shareholder expectations and political climate.
- If successful, this case could be the start of a natural evolution of shareholder and stakeholder activism, becoming more prominent as time goes on. Activist entities may look for potential leverage/arguments in complex, controversial or unproven technologies.

Role in the Energy Transition

The pressure to transform our energy industry is increasing, driven by financial markets, scientific fact, changing consumer expectations, technological advancement and increasing pressure from shareholders and investors. As a result, the pressure on large national and multinational corporations to take action and set net zero goals or commitments is immense.

With the increasing pressure, comes close scrutiny of the structures, planning and evidence in place to reach net zero commitments.

Case in point is the Australasian Centre for Corporate Responsibility's Federal Court proceedings against Santos, the biggest domestic gas supplier in Western Australia. ACCR, a shareholder activist and investor in Santos, commenced proceedings against the oil and gas major in what is reported as the first case in the world to challenge the veracity of a company's net zero target.¹

Proceedings against Santos

On 26 August 2021, the Australasian Centre for Corporate Responsibility ("ACCR") commenced proceedings in the Federal Court of Australia against Santos, reportedly alleging misleading and deceptive conduct and misrepresentations in breach of the *Corporations Act 2001* (Cth) and the Australian Consumer Law (Schedule 2 to the *Competition and Consumer Act 2010* (Cth)).²

In particular, ACCR alleges Santos made representations in its 2020 Annual Report that its natural gas is a "clean fuel" and provides "clean energy", but without disclosing that the processing of natural gas releases significant quantities of carbon dioxide and methane.³

ACCR also alleges that Santos made statements in its 2020 Annual Report that it had a "clear and credible" plan to achieve net zero scope 1 and 2 emissions by 2040; but Santos' expansion of its natural gas operations means that it will increase its greenhouse gas emissions, and its net zero plans depend on a range of undisclosed qualifications and assumptions about carbon capture storage processes and the production of blue hydrogen.⁴

¹ Australasian Centre for Corporate Responsibility, Media release: 'Australasian Centre for Corporate Responsibility files landmark case against Santos in Federal Court', 26 August 2021, <https://www.accr.org.au/news/australasian-centre-for-corporate-responsibility-files-landmark-case-against-santos-in-federal-court/>

² Ibid. See also, Environmental Defenders Office, 'World-first Federal Court case over Santos' 'clean energy' & net zero claims, 26 August 2021, <https://www.edo.org.au/2021/08/26/world-first-federal-court-case-over-santos-clean-energy-net-zero-claims/>

³ Ibid.

⁴ Ibid.

What is the problem with greenwashing and net zero claims particularly? How to manage risk.

Greenwashing is, broadly, the exaggeration or false statements of a company's green or environmental credentials. It will likely capture net zero targets.

Greenwashing risks breaching the Australian Consumer Law or the Corporations Act as misleading or deceptive conduct or as misrepresentations as to future matters.

Inaccurate disclosures about a company's environmental credentials may amount to misleading or deceptive conduct in breach of the Australian Consumer Law or the Corporations Act, if the conduct leads a consumer into error, regardless of intention.

Additionally, representations about future claims that are made without reasonable grounds could amount to misleading or deceptive conduct. The reasonable grounds need to be there at the time the company makes the statement.

Identifying and actioning climate change is a part of the energy transition. But how is the risk of greenwashing managed?

- Companies claiming net zero targets should at least have published plans. But that's not all.
- Those plans and representations need to be appropriately qualified and assessed.
- If a company is making a net zero claim, against which standard is that claim to be assessed? With multiple standards being launched every day, in the absence of mandatory requirements, voluntary adoption of GHG standards should be based on articulated reasoning, a clear vision of how the commitment is to be achieved and a realistic progressive adoption of that pathway.
- Relying on independent, science based targets is a start; but their significance cannot be overplayed. This is particularly in the absence of international standards. And which makes the position all the more difficult for companies in assigning a target based on credible, verified processes.
- Furthermore, if those companies are listed companies, the listing requirements of the markets on which they are listed may also dictate disclosure requirements and standards, including on what sort of claims they are entitled to make.

What is really interesting (and for many, concerning) about the ACCR proceedings is that it builds on current debate in the industry about the use of and reliance on blue hydrogen and carbon capture storage as a means of decarbonisation. Some claim it is worse for the environment than burning natural gas, because of the fugitive emissions for blue hydrogen resulting from an increased use of natural gas to power carbon capture technology. Others are of the view that all technology and innovation has a place, and it is a good and sensible stepping stone to green hydrogen.

From a legal perspective, what is important is that:

- If a company is relying on technology as a means to achieve its net zero target, then advancements in those technologies, or proper and balanced discredit of those technologies or consideration of new technologies may mean that a company will need to update and revise its net zero target or messaging and qualifications/assumptions around that target.
- Companies understand the difficulty they are grappling with – embracing innovation, but having credible grounds to rely on those innovations at the same time. Otherwise, a potential ground for misrepresentation or misleading or deceptive conduct?
- A company's operating structure should link back and reflect the company's net zero target. If products and processes are not put in place to meet the net zero target, then if ever a greenwashing claim is brought, the company may not have the evidence of reasonable grounds it needs to support its net zero commitment.
- It is often said that 'net zero is a journey and not a destination'; therefore, ensuring the organisation as a whole is on that journey together, is fundamental to its success. This should be reflected in the policies and procedures of the organisation, especially the remuneration policies of the directors and employees of the organisation at every
- level. It is likely that a true net zero journey will require a complete overhaul of that organisation's approach to its internal 'key performance indicators' to drive appropriate behaviour and consistent change.
- Look at the business and its operations as a whole when considering net zero targets. How can one division fly the net zero flag when the larger business model is not changing?

HFW plays a key role in the energy transition narrative. We believe all companies have a role to play in the energy transition. It is not about winners and losers – but all making reasonable, flexible, evidence based efforts to change our industry for the better. Talk to us if you would like to know more about the energy transition, properly framing net zero commitments, and playing your part in the transition while managing risk.

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