Vinson&Elkins

Consideration of Climate Change Risks in Government Acquisitions: What You Need to Know

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Today's Presenters

Daniel P. Graham

Partner – Daniel P. Graham

Washington

+1.202.639.6652

danielgraham@velaw.com

Margaret E. Peloso

Partner – Environmental & Natural Resources

New York & Washington

1.202.639.6774

mpeloso@velaw.com

Matthew X. Etchemendy

Counsel – Appellate

Washington

+1.202.639.6740

metchemendy@velaw.com

Today's Presentation

- Biden EO14030 Directive to the FAR Council
- Current FAR dockets on climate issues
- How other decisionmakers account for greenhouse gases and climate risk
  - Social Cost of Carbon
  - Federal Flood Risk Management Standard
- How some companies address their climate risk profiles
  - Voluntary Reporting Frameworks
  - SBTi
  - Net Zero Commitments
- Approaches the FAR Council may take
- Practical Steps to take now

EXECUTIVE ORDER 14030

Biden EO14030 Directive to the FAR Council

- May 20, 2021, President Biden signed EO14030 on Climate-Related Financial Risk, which, in part, addressed Federal Lending, Underwriting, and Procurement
  - Specifically, the FAR Council, in consultation with the Chair of the CEQ and the heads of other agencies, is directed to consider amending the Federal Acquisition Regulations:
    - Public Disclosures & Targets: require major Federal suppliers to disclose GHG emissions and climate-related financial risk and set science-based reduction targets
    - Minimize Risk of Climate Change in Federal Agency Procurements: inclusive of consideration of the social cost of GHG emissions and, where appropriate and feasible, give preference to bids/proposals with a lower social cost of GHG emissions
    - Integration of Climate-Financial Risks: as related to Federal lending policies and programs of the Department of Agriculture, Department of Housing and Urban Development, and the Department of Veterans Affairs (e.g., into underwriting standards, loan terms and conditions, asset management and servicing procedures)

Biden EO14030 Directive to the FAR Council *(cont'd)*

- Additionally, EO14030 directed:
  - The heads of agencies to submit to the Director of OMB, the National Climate Task Force, and the Federal Chief Sustainability Office, actions taken to integrate climate-related financial risk into their procurement processes, consistent with EO14008 (Tackling the Climate Crisis at Home and Abroad) requiring Climate Action Plans (and subsequent interim instructions relating to the same)
    - In relation to this, the Director of OMB and the Federal Chief Sustainability Officer are directed to provide guidance to agencies on existing voluntary standards for use in the agencies' Climate Action Plans
    - Some agencies have released their Climate Action Plans
      - E.g., the U.S. Department of the Treasury, which integrated "climate action planning topic areas." These included "climate vulnerabilities assessment" determining the anticipated climate threat, the recommended adaptation act, the resources needed, the timeline and performance metrics to address each vulnerability, and the disclosures in financial reporting and integration into enterprise risk management processes to be made.
  - The reinstatement of EO13690 (Establishing a Federal Flood Risk Management Standard and a Process for Further Soliciting and Considering Stakeholder Input)

Current FAR Dockets on Climate Issues

- FAR Case No. 2021-015, Disclosure of Greenhouse Gas Emissions and Climate-Related Financial Risk
  - The Defense Acquisition Regulations Council tasked the Acquisition Environmental and Contract Management Team to draft a proposed FAR rule
  - Due date of report extended to November 24, 2021*
- FAR Case No. 2012-016, Minimizing the Risk of Climate Change in Federal Acquisitions
  - October 15, 2021, the FAR Council published an Advance Notice of Proposed Rulemaking in the Federal Register (86 FR 57404)
  - Broadly, the Notice seeks public comment on the incorporation of GHG emissions information into the Federal procurement process and use of the Federal procurement process to mitigate climate-related financial risks

* Source: *Open FAR Cases as of November 01, 2021*, https://www.acq.osd.mil/dpap/dars/opencases/farcasenum/far.pdf

More on FAR Case No. 2012-016

The Notice seeks feedback on several questions, to include:

- *"How can greenhouse gas emissions, including the social cost of greenhouse gases, best be qualitatively and quantitatively considered in Federal procurement decisions, both domestic and overseas? How might this vary across different sectors?"*
- *"What are usable and respected methodologies for measuring the greenhouse gases emissions over the lifecycle of the products procured or leased, or of the services performed?"*
- *"How can procurement and program officials of major Federal agency procurements better incorporate and mitigate climate-related financial risk? How else might the Federal Government consider and minimize climate-related financial risks through procurement decisions, both domestic and overseas?"*
- *"How would (or how does) your organization provide greenhouse gas emission data for proposals and/or contract performance?"*
- *"How might the Federal Government best standardize greenhouse gas emission reporting methods? How might the Government verify greenhouse gas emissions reporting?"*
- *"How might the Federal Government give preference to bids and proposals from suppliers, both domestic and overseas, to achieve reductions in greenhouse gas emissions or reduce the social cost of greenhouse gas emissions most effectively?"*
- *"How might the Government consider commitments by suppliers to reduce or mitigate greenhouse gas emissions?"*
- *"What impact would consideration of the social cost of greenhouse gases in procurement decisions have on small businesses, including small disadvantaged businesses, women-owned small businesses, service-disabled veteran owned small businesses, and Historically Underutilized Business Zone (HUBZone) small businesses? How should the FAR Council best align the objective with efforts to ensure opportunity for small businesses?"*

These questions highlight the potentially pervasive and sweeping scope of changes that FAR could implement, which could raise new enforcement risks under the False Claims Act.

Comments on the proposed rule are due by December 14, 2021.

Existing FAR Part 23 Provisions Involving the Environment and Climate Change

- FAR subpart 23.1—Requires that 95% of new contract actions involve products that are: (1) energy-efficient; (2) biobased; (3) non-ozone depleting; (4) water-efficient; (5) non-toxic or less toxic alternatives; or (6) made with recovered materials
- FAR subpart 23.2—Federal agencies must acquire energy-efficient products and are encouraged to utilize energy-savings performance contracts
  - Contracts under this subpart must include FAR 52.223-15, which requires contractors to “ensure” that energy-consuming products are energy efficient products
- FAR subpart 23.7—Directs agencies to meet additional environmental objectives through the acquisition process, including cost-effective waste reduction and obtaining hazardous waste minimizing products and services
  - FAR clause 52.223-10 requires contractors to establish a program to promote cost-effective waste reduction under the contract and comply with Federal, state, and local environmental requirements during contract performance.

Existing FAR Part 23 Provisions Involving the Environment and Climate Change

- FAR subpart 23.4—directs agencies to develop and implement affirmative procurement programs to purchase products composed of the highest percentage of recovered (recycled) material or biobased content practicable.
  - Incorporates EPA and USDA standards for the minimum amount of recovered material or biobased content in designate items, and agencies must implement a program to require contractors to provide reasonable estimates, certification, and verification of recovered material used in the performance of contracts.
  - FAR 52.223-1 requires contractors to certify that biobased products, as defined by the USDA, will be used or delivered in performance of the contract
  - FAR 52.223-4 requires contractors to certify that the percentage of recovered materials for EPA-designated content will be at least the amount required under the contract.
- FAR subpart 23.8—directs agencies to minimize the procurement of materials and substances that contribute to the depletion of stratospheric ozone and give preference to the procurement of alternative chemicals.
  - FAR 52.223-11 requires contractors to track the amount of ozone-depleting substances contained in equipment delivered to the Government under the contract and annually report that amount to the Government during the contract's performance.
  - FAR 52.223-22 requires contractors to publicly disclose greenhouse gas emissions and reduction goals.

What Approaches Might the FAR Council Take To Implement EO14030?

- Limit to acquisitions solely/predominantly for supplies?
  - EO14030 refers to “major Federal suppliers” with respect to potential GHG emissions disclosure and SBT requirements and discusses potential preferences for “bids and proposals from suppliers with a lower social cost of greenhouse gas emissions”
  - October 15 Advance Notice’s questions not clearly limited to suppliers/acquisitions of supplies
- Establish GHG and SCC goals at the agency level, contractor level, or procurement level?
- Continue FAR Part 23’s focus on contractor self-certification or leverage existing third-party standards and assessment regimes?
- Make GHG emission disclosure and SBT setting a matter of present responsibility or a pass/fail evaluation factor?
  - May not address EO14030’s separate requirement that the FAR Councils consider minimizing the risk of climate change, including by giving preferences to contractors with lower SCC, which implies a qualitative comparison of offerors in individual procurements

ACCOUNTING FOR GHGS AND CLIMATE RISK

How Do Other Decisionmakers Account for GHGs and Climate Risk?

- Qualitative evaluation
- Social Cost of Carbon
- Federal Flood Risk Management Standard

How Do Other Decisionmakers Account for GHGs and Climate Risk? *(cont'd)*

- Qualitative evaluation
  - Quantify expected GHG emissions attributable to the proposal
  - Compare to relevant benchmarks: decisionmaker may refer to state, national, or global emissions levels, or government emissions targets or carbon budgets
  - Assess scale of new GHG emissions in comparison to benchmarks, and qualitatively assess impacts of global climate change

How Do Other Decisionmakers Account for GHGs and Climate Risk? *(cont'd)*

- Social Cost of Carbon
  - Estimates are dollar-value figures meant to estimate the present-value, monetized cost of one additional ton of carbon dioxide into the atmosphere
  - Essentially, it is meant to estimate, in "monetized" terms, how much it is worth to us *today* to avoid the damage projected for the *future*
  - Developed in response to pressure from courts, in 2008 onward, to incorporate effects of regulatory proposals on global greenhouse gas emissions (and thus global climate change) in regulatory cost-benefit analyses under EO12866
  - How does it work?
    - Average inputs taken from three "Integrated Assessment Models" produced by economists: FUND (Richard Tol), DICE (William Nordhaus), and PAGE (Chris Hope)
    - Integrate (physical) climate sensitivity estimates and human/social damages estimates
    - The Integrated Assessment Models are run under the assumption of X emissions, then X+1, to get a per-ton figure

How Do Other Decisionmakers Account for GHGs and Climate Risk? *(cont'd)*

- Social Cost of Carbon *(cont'd)*
  - Factors included in social cost of carbon calculations:
    - Socioeconomic predictions (e.g., population growth over a given future year, future energy-usage patterns)
    - Climate projections (e.g., how fast will sea levels rise?)
    - Benefits and costs (e.g., how much will sea level rise cost?)
    - Discount rate (the rate at which a decisionmaker is willing to trade present benefits/costs for future ones; a policy judgment—widely proposed values range from 0% to 7%)
  - Problems:
    - Information utilized is uncertain and models are unverifiable/unfalsifiable (at present time)
    - Damages estimates are largely non-scientific (by necessity)
    - Policy-based judgments, such as choice of discount rate, can make order-of-magnitude differences in cost estimates

How Do Other Decisionmakers Account for GHGs and Climate Risk? *(cont'd)*

- Federal Flood Risk Management Standard
  - Issued January 2015 to "encourage federal agencies to consider current and future risk when taxpayer dollars are used to build or rebuild near floodplains"
    - Designed to assist in reducing the risk and cost of future flood disasters by ensuring investments in, and those affecting floodplains, are well constructed to withstand impacts of flooding
    - Standard is required for federally funded projects ("actions where Federal funds are used for new construction, substantial improvement, or to address substantial damage to a structure or facility")
  - Revoked by the Trump Administration in 2017
  - Reinstated by the Biden Administration in January 2021

How Do Other Decisionmakers Account for GHGs and Climate Risk? *(cont'd)*

- Federal Flood Risk Management Standard *(cont'd)*
  - Eight step decision-making process:
    1. Determine if a proposed agency action is located in a floodplain
    2. Notify the public of proposed action
    3. Identify and evaluate practicable alternatives
    4. For proposed alternatives, identify if the action has impacts in a floodplain *or* directly or indirectly supports floodplain development that has additional impacts
    5. If above is met, identify minimization of effects and how natural and beneficial floodplain values can be restored and preserved
    6. Revaluate proposed alternatives accounting for the above
    7. Notify the public if agency finds only practicable alternative is locating in a floodplain (to include reasons for this finding)
    8. Allow for public response, then implement proposed action

CLIMATE RISK PROFILES

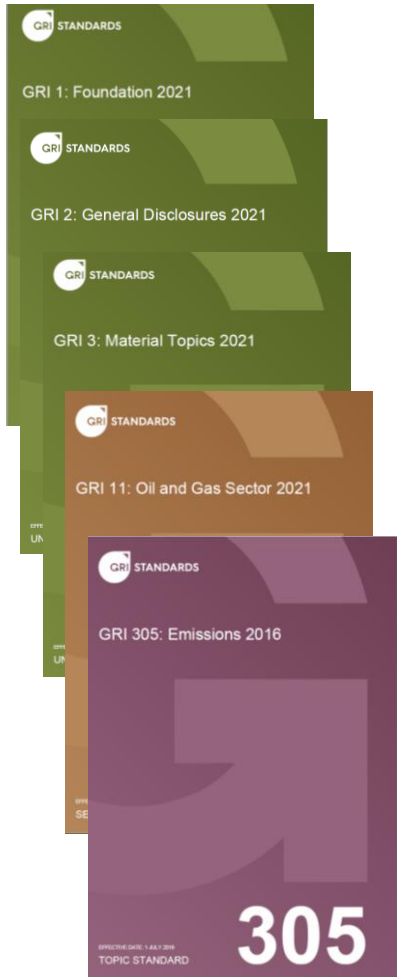
How are Companies Addressing their Climate Risk Profiles?

- Voluntary Reporting Frameworks → designed to help organizations effectively disclose climate-related risks and opportunities
  - TCFD (Taskforce on Climate-Related Financial Disclosures):
    - Four thematic areas: governance; strategy; risk management; metrics and targets
      - **Governance**: organization's governance around climate-related risks and opportunities (board oversight and management's role)
      - **Strategy**: actual and potential impacts of climate-related risks and opportunities on an organization's strategy, business, and financial planning (short-, medium-, and long-term risks and consideration of resilience, inclusive of climate-related scenarios; e.g., a 2°C or lower scenario)
      - **Risk Management**: processes used by organizations to identify and manage climate-related risks (physical and transitional)
      - **Metrics and Targets**: used to assess and manage climate-related risks and opportunities (e.g., Scope 1, 2, and 3 emissions, disclosure of targets)

TCFD | TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES

How are Companies Addressing their Climate Risk Profiles? *(cont'd)*

- GRI (Global Reporting Initiative):
  - Modular system comprising three series of Standards: the GRI Universal Standards; the GRI Sector Standards; and the GRI Topic Standards
    - **GRI Universal Standards**: applicable to all organizations using the GRI to voluntarily report information Consists of:
      - GRI 1: Foundation – outlines purpose of the Standards and explains how to use the Standards
      - GRI 2: General Disclosures – disclosures relating to an organization's structure and reporting practices; governance; strategy; policies; activities and workers; practices; stakeholder engagement
      - GRI 3: Material Topics – explains how an organization determines its material topics—those most relevant to its impacts—and how the Sector Standards are used in this process. Contains disclosures for reporting on the material topics
    - **GRI Sector Standards**: intended to "increase the quality, completeness, and consistency of reporting" Standards are to be developed for 40 sectors. Currently have GRI Sector Standard for Oil & Gas
    - **GRI Topic Standards**: includes disclosures for providing information on topics such as waste, safety, tax, and occupational health. Topic Standards selected to correspond to an organization's material topics



How are Companies Addressing their Climate Risk Profiles? *(cont'd)*

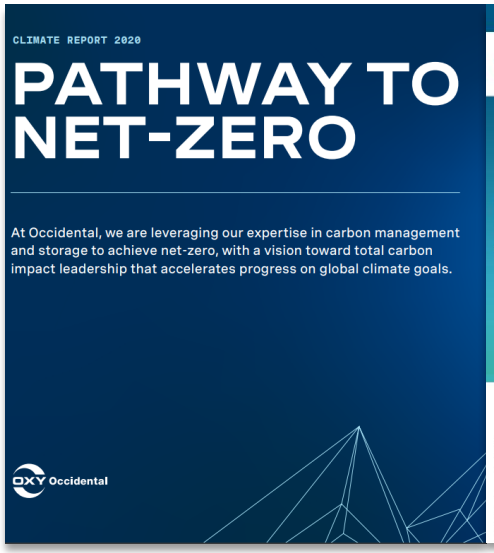
- SASB (Sustainability Accounting Standards Board):
  - Complete set of 77 Industry Standards (consumer goods; extractives & minerals processing; financials; food & beverage; health care; infrastructure; renewable resources & alternative energy; resource transformation; services; technology & communications; transportation)
  - Each Standard identifies environmental, social, and governance issues most relevant to the financial performance in each of the industries which are designed to help an organization disclose financially material sustainability information
  - SASB Implementation Supplement to address Greenhouse Gas Emissions offers guidance on disclosure of Scope 1, 2, or 3 emissions
  - SASB Human Capital Bulletin provides an overview of human capital-related topics and metrics to help an organization prepare human capital-related disclosures required by the SEC

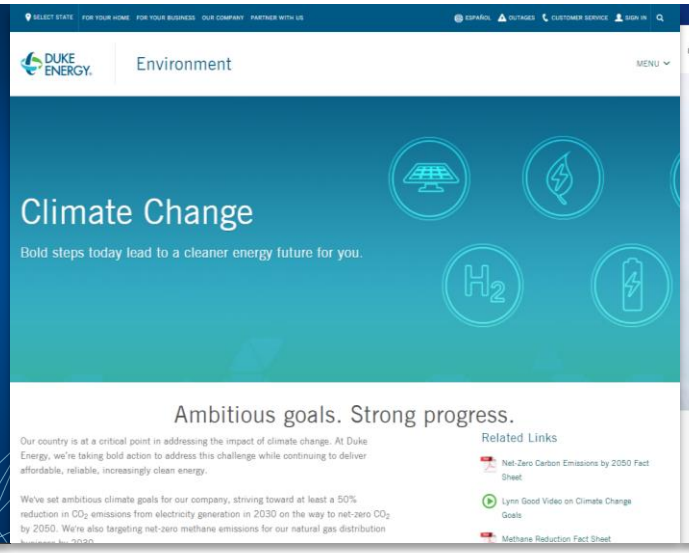
How are Companies Addressing their Climate Risk Profiles? *(cont'd)*

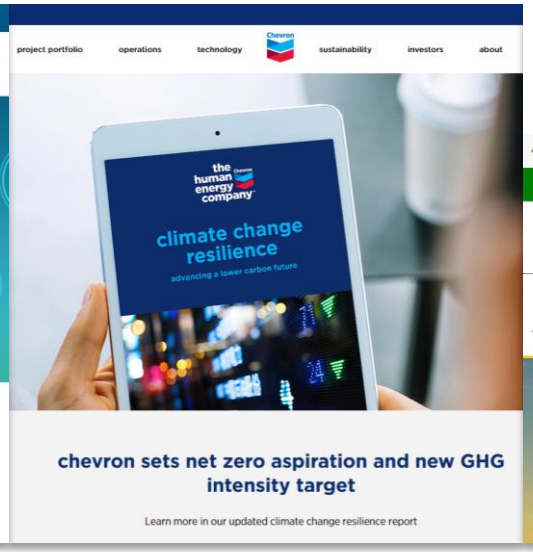
- Science Based Target Initiative (SBTi) → designed to aid organizations willing to commit to setting a science-based target
  - Provides a "clearly-defined path" to reducing greenhouse gas emissions in line with the goals of the Paris Agreement
    - Targets are "science based" if they are in line with the latest climate science determined to be necessary to meet the goals of the Paris Agreement (limiting global warming to below 2°C above pre-industrial levels; pursuing limiting global warming to 1.5°C)
  - Five-step process:
    - **Commit**: intent to set a science-based target through submission of a letter
    - **Develop**: using SBTi criteria, work on an emissions-reduction target
    - **Submit**: present the target to SBTi for official validation
    - **Communicate**: announce the target and inform stakeholders
    - **Disclose**: track progress annually and report on company-wide emissions

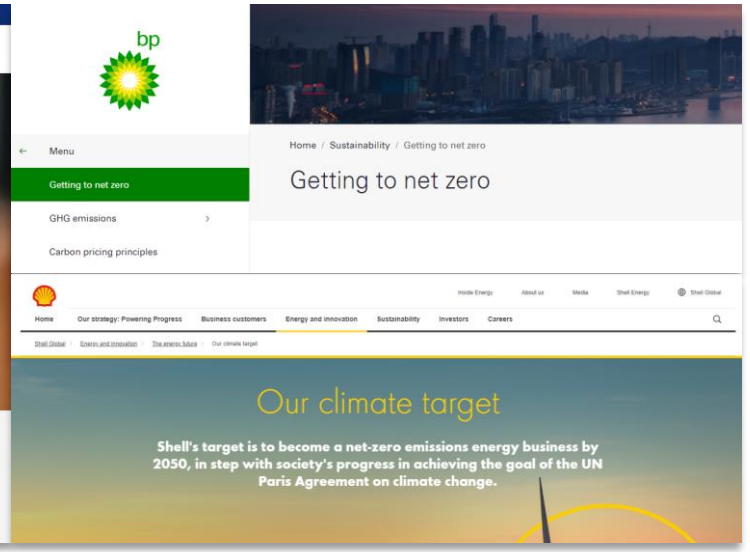
How are Companies Addressing their Climate Risk Profiles? *(cont'd)*

- Net Zero Commitments → increasingly popular for organizations to commit to achieve net zero greenhouse gas emissions in their operations by a deadline (e.g., 2030, 2050)
  - Reducing emissions or balancing new emissions. Designed to limit global temperature rises to 1.5°C
  - March 2021, approximately one-fifth of the world's 2,000 largest public companies have committed to net zero targets (representing sales of nearly $14 trillion)
  - Not just public companies but private companies too and countries
    - E.g., the U.K.'s Net Zero Strategy: Build Back Greener









PRACTICAL STEPS TO TAKE NOW

Getting Ready – Practical Steps to Take Now

- Assess the current state of your climate data and reporting program (if any)
  - Do you have the information and systems in place to provide climate-related data the FAR Council may require?
  - Is your current voluntary reporting preparing you for future regulation? Does it create any vulnerabilities?

- Evaluate your ESG Governance
  - Do you have the processes and procedures in place to validate your climate data and progress towards any climate goals?
  - Are you creating appropriate documentary records to substantiate your climate claims?

- Consider climate reporting frameworks and science-based targets (preliminary assessment to know what you'll need to do when the final FAR Council rules take shape)

- Determine if there are key data gaps or implementation issues that should be raised in comments to the FAR Council

Questions?

Daniel P. Graham

Partner – Daniel P. Graham

Washington

+1.202.639.6652

danielgraham@velaw.com

Margaret E. Peloso

Partner – Environmental & Natural Resources

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mpeloso@velaw.com

Matthew X. Etchemendy

Counsel – Appellate

Washington

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metchemendy@velaw.com

THANK YOU

Austin
T +1.512.542.8400

Dallas
T +1.214.220.7700

Dubai
T +971.4.330.1800

Houston
T +1.713.758.2222

London
T +44.20.7065.6000

Los Angeles
T +1.213.527.6400

New York
T +1.212.237.0000

Richmond
T +1.804.327.6300

Riyadh
T +966.11.250.0800

San Francisco
T +1.415.979.6900

Tokyo
T +81.3.3282.0450

Washington
T +1.202.639.6500