JONES DAY

ESG Roadmap: Real Impacts on Real Property and Infrastructure

Environmental, Social & Governance ("ESG") has become an integral part of business for participants in the real estate and infrastructure sectors, and a mandatory investment criterion for many capital sources. This roadmap provides a snapshot of the key drivers of integration of ESG principles in the real estate and infrastructure sectors and highlights paramount issues for stakeholders across the globe.

Drivers of ESG

ESG-related focus in the real estate and infrastructure industries centers on three key drivers: (i) demand from investors and fund sponsors; (ii) financial risk management; and (iii) an increasingly rigorous regulatory landscape.

Market Demand	Financial Risks	Regulatory Shifts

MARKET DEMAND

Investors and fund sponsors, especially those with ESG-related commitments, commonly consider a company's ESG policies to ensure that a target business can withstand the effects of climate-related events; attract and retain management, tenants, and customers; ensure responsible human rights practices; mitigate financial risk; and appropriately set, monitor, and report the company's stated ESG goals and progress. As a result, real estate- and infrastructure-focused companies face pressure to perform ESG-risk due diligence and assess, implement, and govern their ESG policies.

Jones Day regularly advises key stakeholders in ESG-related due diligence and strategic planning to account for the complex factors that may impact financial and enforcement risks.

FINANCIAL RISK

In respect of financial risk management, stakeholders face pressure to hedge climate-related physical and transitional risks. Physical risks can carry significant capital costs. For example, climate-related disasters can result in substantially higher insurance premiums, increase operational costs, and erode the value of buildings and other infrastructure. Transitional risks—i.e., economic, political, and social responses to climate-driven shifts—can also be costly due to the pricing-in of carbon emissions (through carbon taxes and pricing schemes), market impacts, supply chain disruptions, energy and technological inefficiencies, regulatory responses, and other legal and reputational risks.

Jones Day has extensive experience advising on virtual power purchase agreements, sleeved retail renewable energy purchase agreements, community solar agreements, demand response agreements, carbon credit agreements, energy storage agreements, and related data analytic agreements, as well as energy transition transactions resulting in zero-carbon or zero-net-carbon physical assets.

REGULATORY SHIFTS

At least 16 U.S. states require the reduction of greenhouse gas emissions, and more states have emissions reporting and/or inventory requirements. Washington D.C.'s CleanEnergy DC Omnibus Act requires commercial and multifamily buildings to improve energy performance by 20% over a five-year compliance period. New York City passed Local Law 97 requiring most buildings over 25,000 square feet to meet energy efficiency and GHG limitations by 2024. Further, the Biden administration requires the federal government to develop or adopt building emissions standards, and set a goal for all federal buildings in its portfolio to achieve a 50% emissions reduction by 2032 and to reach net-zero emissions by 2045. California's Climate Accountability Package, the most aggressive state regulation to date, jumpstarts climate reporting requirements as early as 2026, including Scope 3 emissions. Natural gas connections in new construction also are restricted in some locations.

> **"The future is now when it comes to ESG strategy. Decisions made today will impact companies for decades to come."**
>
> — **Brian Sedlak**, *Jones Day*

Jones Day provides clients with valuable insights using "gap analyses," which help identify the potential scope of the application of these rules (e.g., considering complex areas like the application to joint ventures and minority investments). We also help identify key areas in which changes to internal policies or procedures are required, additional corporate disclosures are needed, or required data is lacking.

Investors and project sponsors need also consider whether regulations from beyond U.S. borders impose ESG-related obligations or restrictions on investment activity. Australia, the European Union, Canada, and Switzerland are among the jurisdictions with far-reaching ESG-related rules that may impact U.S. and non-U.S. investors alike.

Key Stakeholders

Key stakeholders in the real estate and infrastructure sectors—including users and operators, investors, and fund sponsors—face challenges in navigating pitfalls and leveraging opportunities to align businesses with ESG principles. Jones Day counsels global clients by providing tailored advice in virtually all areas of law that concern real estate and infrastructure, including corporate, M&A, financing, litigation and disputes, regulatory, energy, tax, labor and employment, and more. Our lawyers focus on jurisdictions and disciplines that matter to clients to maximize ESG-related opportunities while piloting ESG-related risk.

CORPORATE, M&A, AND FINANCING

Owners should consider "responsible divestment," i.e., taking steps when divesting or disposing of assets that are poor or underperforming from an ESG metrics perspective to ensure that future owners will manage the assets consistent with the seller's ESG commitments by, e.g. retrofitting and repurposing those assets. There are an increasingly large number of asset managers acquiring brown assets for retrofitting and/or repurposing, particularly motivated by recent developments in state and federal incentives programs.

Jones Day assists clients with initial structuring, equity capital raising, project level debt financing, and project level joint venture formations for real estate and infrastructure businesses.

Green bonds (i.e., conventional bonds whose proceeds are earmarked for green investments) have become a popular financing tool because they align the interests between capital providers and ESG stakeholders seeking carbon-efficient buildings and energy sources. In addition, green bonds enable businesses to receive funding to develop and/or retrofit real estate and infrastructure projects, and investors are able to meet portfolio ESG mandates.

Jones Day's experience includes advising on green bonds and sustainability-linked financings.

LITIGATION AND DISPUTES

As stakeholders seek to meet high ESG-related expectations from investors and sponsors, it is paramount to manage any risk of costly greenwashing claims (i.e., the overstatements of ESG-related impacts of products or services). Disputes have increased recently in this area.

Jones Day regularly advises key stakeholders on ESG-related litigation and enforcement, potential personal liability for directors, and implementing effective and meaningful policies to mitigate such risks, as well as investigating and responding to claims if and when they arise.

REGULATORY, ENERGY, AND TAX

In furtherance of the green transition, both U.S. federal and state governments offer billions of dollars in financing and incentives to incorporate ESG principles into real property and infrastructure projects. Particularly, the Inflation Reduction Act and the Infrastructure Investment and Jobs Act both earmark significant resources in the form of tax credits and loan guarantees to incentivize efforts to reduce carbon emissions and electrify energy infrastructure.

Jones Day represents numerous clients in connection with maximizing state and federal incentives through, for example, implementing complex tax equity structures that take full advantage of tax credits and project development and construction loans.

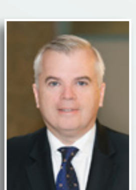
Human rights issues, responsible labor practices, and diversity, equity, and inclusion are just a few examples of the "S" and "G" in ESG. There is significant pressure on stakeholders to ensure that risks associated with anti-slavery, anti-bribery, anti-money laundering, data protection, and sanctions principles are effectively managed up and down the business supply chain.

> **"We are focused on identifying real opportunities for clients to achieve their ESG objectives in real estate and infrastructure."**
>
> — **Chuck Wehland**, *Jones Day*

Jones Day advises in-house counsel and boards of directors in the real estate and infrastructure sectors in developing and implementing social and governance protocols, including advising on employment issues such as the gender pay gap, as well human rights due diligence and supply chain management.

CLICK HERE to explore Jones Day's detailed ESG-related analyses of the real estate and infrastructure sectors.

Contacts



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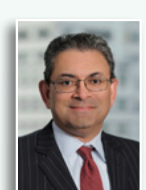

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