29 August 2022

The Trustee for Unisuper
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Dear Unisuper Trustees,

RE: UNISUPER'S INVESTMENTS IN SANTOS MAY AMOUNT TO A BREACH OF THE LAW

1. The EDO acts on behalf of Rachel Davies who is a member of Unisuper.

Summary of member concerns

2. The purpose of this letter is to set out our client's concerns that by continuing to invest members' funds in oil and gas companies (namely Santos), the Trustees of Unisuper and its directors may be in breach of their obligations under section 52[1] of the *Superannuation Industry (Supervision) Act 1993* (Cth) (**SIS Act**) (**Trustee breaches**) and s 52A(2) of the SIS Act (**Director breaches**). These potential breaches arise as a result of how the Trustee is managing the climate risks to the fund. In particular:

    a. Unisuper's own climate plan may not be Paris Agreement[2]-aligned (**Paris-aligned**) because it focuses on "a well below 2 degrees" warming limit rather than 1.5 degrees, and it fails to include Scope 3 emissions (**Issue 1**);

    b. Unisuper has failed to adequately interrogate the net zero claims/emissions reduction representations made by companies in which member funds are invested, namely Santos (**Issue 2**);

    c. Unisuper has recently voted against shareholder proposals requesting Santos to disclose plans for how it will align its capital allocation to oil and gas assets with a net zero by 2050 and Paris-aligned scenario[3] (**Issue 3**);

    d. According to its latest portfolio holdings disclosure,[4] Unisuper had $163.8 million invested in Santos, with over $110 million of this invested through the "Balanced" option, which is Unisuper's default Mysuper option. Unisuper has failed to divest from Santos (**Issue 4**) despite the fact that it knew, or ought to have known, that:

[1] Subsections (2),(6),(8)(a).
[2] United Nations Framework Convention on Climate Change, May 9, 1992, S. Treaty Doc. No. 102-38.
[3] As voted on in the Santos 2021 and 2022 AGMs.
[4] Dated 31 December 2021.

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i. Santos is expanding its oil and gas production in a manner that is inconsistent with the climate goals of the Paris Agreement and a net zero emissions by 2050 pathway; and

ii. continued investment in companies such as Santos pursuing new oil and gas projects is an investment in a stranded asset that creates an unreasonable financial risk to members in the long term.

3. Our client is also concerned that Unisuper may also have engaged in misleading or deceptive conduct under s 1041H of the *Corporations Act 2001* and ss 12DA, 12DB(1)(a) and (e) of the *Australian Securities and Investment Commission Act 2001* (Cth) (**ASIC Act**) by making a number of representations (set out in **Annexure A**) which, alone or in combination, convey that:

   a. Unisuper is a leader on climate action;

   b. Unisuper's corporate and investment strategy are aligned with the Paris Agreement;

   c. Unisuper is reducing its portfolio emissions and aims to reach net zero by 2050;

   d. Unisuper's investment strategy (including its consideration of climate) will help deliver long-term value for Unisuper members;

   e. Unisuper is committed to reducing its environmental impact; and

   f. Unisuper has been engaging with those companies in which it is invested (including Santos) to transition them in line with the Paris Agreement.

   (collectively, the **Representations**).

4. The Representations are misleading or deceptive or likely to mislead or deceive members or potential members in circumstances where:

   a. Unisuper's own emissions reduction plan may not be Paris-aligned in circumstances where it is aligned to a "well below 2 degrees" rather than 1.5-degree scenario and where it fails to include the Scope 3 emissions of the companies in which it invests in;

   b. Unisuper continues to invest in Santos, which is a major contributor to global warming;

   c. Santos' net zero pathway fails to include a Paris-aligned reduction in scope 3 emissions[5] in circumstances where scope 3 emissions amount to over 85% of the company's total emissions;

   d. Santos' net zero representations are dependent on Carbon Capture and Storage and blue hydrogen (hydrogen produced through the burning of natural gas which is then allegedly abated through carbon capture and storage) that are the subject of a current legal challenge alleging that such representations are misleading or deceptive; and

   e. notwithstanding its apparent net zero representations, Santos has plans to significantly increase oil and gas production, including by pursuing new projects, leading to increased emissions. Such actions are contrary to the International Energy

[5] Scope 3 emissions are defined by the GHG Protocol's Corporate Accounting and Reporting Standard as indirect emissions from a company's upstream and downstream activities and emissions associated with outsourced/contract manufacturing, leases or franchises not included in scope 1 and scope 3 emissions.

Agency (IEA)'s projections under its Net Zero Emissions scenario (**NZE**) that to achieve net zero by 2050 no new oil or gas fields should be approved for development from 2021.[6]

Applicable law

Duties of superannuation trustees

5. As you are aware, section 52 of the SIS Act integrates various mandatory covenants into the governing rules of all super funds. Such covenants relevantly include:

    a. to exercise, in relation to all matters affecting the entity, the same degree of care, skill and diligence as a prudent superannuation trustee would exercise in relation to an entity of which it is trustee and on behalf of the beneficiaries of which it makes investments;

    b. to perform the trustee's duties and exercise the trustee's powers in the best financial interests of the beneficiaries;

    c. to formulate, review regularly and give effect to an investment strategy for the whole of the entity, and for each investment option offered by the trustee in the entity, having regard to, relevantly:

        i. the risk involved in making, holding and realising, and the likely return from, the investments covered by the strategy, having regard to the trustee's objectives in relation to the strategy and to the expected cash flow requirements in relation to the entity;

        ii. the ability of the entity to discharge its existing and prospective liabilities;

        iii. any other relevant matters; and

    d. to exercise due diligence in developing, offering and regularly reviewing each investment option

    (collectively, the **Trustee Duties**).

Duties of directors of corporate superannuation trustees

6. Section 52A of the SIS Act requires that directors of corporate superannuation trustees:

    a. exercise the same degree of care, skill and diligence as a prudent superannuation entity director would exercise;

    b. to perform their duties and exercise their powers in the best financial interests of the beneficiaries;

    c. to exercise a reasonable degree of care and diligence for the purposes of ensuring that the corporate trustee complies with the Trustee Duties

    (collectively, the **Director Duties**).

7. The 2017 Legal Opinion of Noel Hutley SC and James Mack concluded that climate change risk were a material financial risk, and that *"it is incumbent upon a trustee director, in an appropriate case, to consider climate change risk in order to satisfy the requirements of s*

[6] Net Zero by 2050 A Roadmap for the Global Energy Sector. International Energy Agency, May 2021. https://www.iea.org/reports/net-zero-by-2050

52A(2)(b) in relation to due care, skill and diligence, s 52A(2)(c) in relation to the best interests of beneficiaries and at s 52A(2)(f) in relation to ensuring the corporate trustee carries out the s 42 covenants."[7] The supplementary opinion released in 2021 further stated that to discharge their Director Duties, directors of superannuation trustees must understand the risk posed by climate change to investments and manage any identified risk.[8] In particular, *"if a risk is too great for a particular investment objective, a superannuation trustee will need to consider divestment or a reallocation of funds to less risky investment options/asset classes."*[9]

<u>Misleading or deceptive conduct</u>

8. Section 1041H of the *Corporations Act 2001* (Cth) provides that:

   A person must not, in this jurisdiction, engage in conduct, in relation to a financial product or a financial service, that is misleading or deceptive or is likely to mislead or deceive.

9. Section 12DA of the ASIC Act similarly provides that:

   A person must not, in trade or commerce, engage in conduct in relation to financial services that is misleading or deceptive or is likely to mislead or deceive.

10. Section 12DB of the ASIC Act further provides that:

    A person must not, in trade or commerce, in connection with the supply or possible supply of financial services, or in connection with the promotion by any means of the supply or use of financial services:

    (a) make a false or misleading representation that services are of a particular standard, quality, value or grade; or

    …

    (e) make a false or misleading representation that services have sponsorship, approval., performance characterises, uses or benefits.

11. By providing superannuation benefits to members, Unisuper:

    a. "deals in a financial product" within the meaning of s 1041H(2)(a) and s 1041H(2)(b)(vi) and (x)[10]; and

    b. provides a financial service within the meaning of s 12BAB(1)(g) of the ASIC Act[11] in relation to a financial product within the meaning of s 12BAA(7)(f) of the ASIC Act.[12]

12. Conduct is misleading or deceptive or likely to mislead or deceive if *"the impugned conduct viewed as a whole has a tendency to lead a person into error."* This takes into account the conduct in its entirety (including its context) and considers how the conduct affects the

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[7] Noel Hutley SC and James Mack, 2017, "Memorandum of Opinion: Superannuation fund Trustee Duties and Climate Change Risk". Available at: https://www.envirojustice.org.au/sites/default/files/files/20170615%20Superannuation%20Trustee%20Duties%20and%20Climate%20Change%20(Hutley%20%26%20Mack).pdf; at [10].

[8] Noel Hutley SC and James Mack, 2021, "Memorandum of Opinion: Superannuation fund Trustee Duties and Climate Change". Available at: https://equitygenerationlawyers.com/wp/wp-content/uploads/2021/04/Hutley-SC-Mack-Superannuation-Trustee-Duties-and-Climate-Change-Memo-2021.pdf at [5].

[9] Ibid, at [7].

[10] *Australian Securities and Investments Commission v MLC Nominees Pty Ltd* [2020] FCA 1306 at [40]

[11] Ibid at [44].

[12] Ibid at [43].

audience's impression of the good or service, which in this case involves how Unisuper invests members' funds.

Trustee and Director Breaches

13. Our client is concerned that Unisuper may be liable for Trustee Breaches and Director Breaches in circumstances where:

Issue 1: Unisuper's climate plan may not be Paris-Aligned

14. In its August 2021 Climate risk and investments report, Unisuper stated that:

> *"while there are several pathways to demonstrate alignment, our targets encourage the following ambition:*
>
> > *To have an even chance of achieving well below 2-degrees ambition, global emissions need to fall by 45% by 2030, and be net-zero carbon by 2050"*

15. We consider it may be misleading or deceptive for Unisuper to represent that its emissions reduction path/climate change plan "Paris-aligned" in circumstances where:

    a. Unisuper's target is based on a "well below 2-degree warming" scenario in circumstances where there has been a refocusing of international and scientific efforts to the 1.5-degree warming goal of the Paris Agreement. Clause 16 of the Glasgow Pact *"Recognizes that the impacts of climate change will be much lower at the temperature increase of 1.5 °C compared with 2 °C, and resolves to pursue efforts to limit the temperature increase to 1.5 °C."* Further, as of July 2021, the Science-Based Targets Initiative (**SBTi**) refuses to accept targets relying on a "well below 2 degrees" scenario and require targets to be set based on a 1.5 degree scenario;[13] and

    b. Unisuper's does not include the Scope 3 emissions of those companies it invests in its carbon footprint calculation.[14] For the reasons set out in paragraphs 24 and 25 below, we consider this to be flawed and not Paris-aligned.

16. See paragraphs 19 and 20 as to further details on what we argue "science-based" and "Paris-align" mean.

Issue 2: Unisuper's failure to interrogate Santos' net zero claims/emissions reduction representations

Santos' net zero/emissions reduction representations

17. As at the date of this letter, Santos' publicly expressed commitments include:

    a. 30% reduction in absolute Scope 1 and 2 emissions by 2030 compared to the Santos and Oil Search combined 2019-20 equity Scope 1 and 2 baseline of 5.9 MtCO2e (**Santos Baseline**);

    b. 40% reduction in the intensity of Scope 1 and 2 emissions by 2030;

    c. achieve net-zero Scope 1 and 2 emissions by 2040;

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[13] https://sciencebasedtargets.org/news/sbti-raises-the-bar-to-1-5-c#:~:text=The%20Science%20Based%20Targets%20initiative,'%20above%20pre%2Dindustrial%20levels

[14] See page 56 of the Unisuper Climate risk and Investments report dated August 2021.

d. use CCS technology to accelerate the economic feasibility of hydrogen and deliver a step change in emissions reduction; and

e. reduce customers' Scope 1 and 2 emissions by at least 1.5 million tonnes per annum of CO_2 emissions by 2030 through the supply of 'clean fuels' (an apparent Scope 3 emissions reduction target).

Unisuper's failures

18. Our client is concerned that Unisuper has failed to interrogate the veracity of Santos' Climate Representations, and that it has incorrectly and unreasonably concluded that Santos has *"already set a science-based net zero target that is aligned with the objectives of the Paris Agreement."*[15]

19. According to the SBTi, a target is "science-based" if it is in line with what the latest climate science deems necessary to meet the goals of the Paris Agreement"[16] i.e. being "Paris-aligned.

20. In circumstances where there is no Australian statutory definition of "Paris-aligned," the general principles of construction apply such that the phrase will need to be interpreted in its context. How other jurisdictions or schemes define "Paris-aligned" may be illustrative. Examples include:

    a. **EU Paris-Aligned Benchmark:** an emission pathway which is consistent with 1.5℃ with no or limited overshoot (IPCC SR15 scenario). An entity's emissions reduction plan must include Scope 3 emissions. [17]

    b. **Science-based Targets Initiative (SBTi):** a 1.5ºC aligned pathway which stays within the 500 GT carbon budget. This requires a 42% reduction in emissions by 2030 from 2020 level and reaching net-zero CO_2 at the global level by 2050.[18] An entity's emissions reduction plan must include Scope 3 emissions.[19]

    c. **International Energy Agency (IEA)'s Net Zero Roadmap (IEA):** which states that:

        i. natural gas demand will decline by 55% in 2050;[20] and

        ii. no new oil and gas fields can be approved for development after 2021.[21]

21. Case law provides that if a statement in its context is likely to be taken as implying that there is an adequate foundation in scientific knowledge for it to be made, then proof that there is no such foundation may render the statement misleading or deceptive.[22] There is significant controversy amongst the scientific community as to whether the use of "negative emission technology" such as Carbon Capture and Storage is able to facilitate Paris-aligned decarbonisation. This is currently the subject of Federal Court Proceedings.[23]

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[15] Page 6 of Unisuper's Responsible Investment Report 2022.
[16] https://sciencebasedtargets.org/how-it-works
[17] https://finance.ec.europa.eu/system/files/2019-12/192020-sustainable-finance-teg-benchmarks-handbook_en_0.pdf
[18] https://sciencebasedtargets.org/resources/files/Pathway-to-Net-Zero.pdf
[19] Ibid.
[20] IEA, 2021, 'Net Zero by 2050: A Roadmap for the Global Energy Sector.' Available at: https://iea.blob.core.windows.net/assets/deebef5d-0c34-4539-9d0c-10b13d840027/NetZeroby2050-ARoadmapfortheGlobalEnergySector_CORR.pdf Page 12.
[21] Ibid.
[22] *Janssen Pharmaceutical Pty Ltd v Pfizer Pty Ltd* (1986) ATPR 40-654 at 47, 293 per Burchett J.
[23] See https://www.edo.org.au/2021/08/26/world-first-federal-court-case-over-santos-clean-energy-net-zero-claim

22. **Santos' Climate Representations are <u>not</u> science-based or Paris-aligned** for the following reasons:

   a. they fail to include a NZE or Paris-aligned Scope 3 emissions reduction target (discussed at paragraphs 24 to 26);

   b. they are heavily reliant on the use of Carbon Capture Utilisation and Storage (CCUS) and blue hydrogen, and therefore may be misleading or deceptive (discussed at paragraphs 28 to 31); and

   c. rather than reducing emissions, Santos is expecting to increase emissions as it invests a significant proportion of its capital to highly-emitting new and expanding gas projects (discussed at paragraphs 32 to 36).

23. Curiously, Santos is notably absent from the table at pages 18 and 19 of its latest August 2021 Climate Risk report setting out Unisuper's consideration of the climate action undertaken by companies in which it invests.[24]

<u>Failure to have a Paris-aligned Scope 3 emissions reduction target</u>

24. Scope 3 emissions are far and away the largest source of emissions for fossil fuel producers. Santos and Oil Search's Scope 3 emissions represented 86.8% of their total emissions in 2021. A failure to have a Paris-aligned Scope 3 emissions plan will render any other action on climate largely meaningless.

25. This is recognised by key metric setting organisations. For instance, to achieve recognition by the Science-Based Targets Initiative, *all* companies involved in the sale or distribution of natural gas and/or other fossil fuels are required to set near- and long-term Scope 3 targets for the use of sold products consistent with the level of decarbonisation required to keep global temperature increase to 1.5 °C.[25] Similarly, the Investor Group on Climate Change's (IGCC) guidance on climate transition plans states that *"fossil fuel producers in particular should set short, medium and long-term targets that apply to Scope 3 emissions."*[26] More recently, the March 2022 exposure draft of the 'IFRS Sustainability Disclosure Standard S2 Climate-related Disclosures' provides that in disclosing information regarding climate-related targets, organisations should state the amount of the entity's emission target to be achieved through emission reductions within the entity's entire value chain (i.e. include scope 3 emissions).

26. Contrary to Unisuper's allegation at page 6 of its Responsible Investment Report, **Santos does not have a target of net zero Scope 3 emissions by 2040**. Santos' net zero by 2040 target is limited to scope 1 and 2 emissions only. Santos has a *2030* target to work with customers to reduce their emissions by 1.5 MtC02e by 2030. This amounts to a mere 3.84% of Santos' 2020-21 Scope 3 equity emissions[27] (on the conservative assumption that there is no change in Santos' scope 3 emissions by 2030), and is woefully inadequate to meet the Paris Agreement. In *Milieudefensie v Royal Dutch Shell,* the Hague District Court found that to meet the Paris

[24] https://www.unisuper.com.au/-/media/files/investments/climate-risk-and-our-investments-2021.pdf?rev=7806e3e0de694bbbae294092937485dc&hash=C9A07DC44DB9D1D0C75EB709BD6F28D6

[25] Science Based Targets initiative. (2021, October). SBTi criteria and recommendation s. (TWG-INF-002) (Version 5.0)[Online]. Available: https://sciencebasedtargets.org/resources/files/SBTi-criteria.pdf

[26] IGCC, Corporate Climate transition plans: A Guide to investor expectations, March 2022. Available at: https://igcc.org.au/wp-content/uploads/2022/03/IGCC-corporate-transition-plan-investor-expectations.pdf

[27] Santos reported Scope 3 equity share emissions (use of sold products) in 2020-2021 of 39 MtCo2e.

Agreement, a reduction target of 45% in CO_2 scope 1, 2 and 3 emissions by 2030 relative to 2010 was required.[28]

27. Further, rather than committing to a percentage reduction in Scope 3 emissions as per the industry guidance, Santos has committed to reducing customers' Scope 1 and 2 emissions by 1.5 million tonnes per annum of CO_2e by 2030. This is problematic because certification and industry bodies do not accept targets that specify reduction by a mass of GHGs because they fail to provide accurate and comparable data on emissions reduction. The SBTi states that *"companies shall not set targets to reduce emissions by a specified mass of GHGs (e.g., "to reduce emissions by 5 million tonnes by 2030") or targets that benchmark performance against sector average values. This is because such targets are not transparent about changes in emissions performance. Also, sector-benchmarked targets may also change over time with changes in sector performance, reducing the ability to track long-term changes in performance."*[29]

<u>Santos 'reliance on CCS and blue hydrogen</u>

28. Santos relies on unproven CCS technology and blue hydrogen (which it has controversially referred to as "clean energy") to achieve its emissions reduction targets. These representations are currently the subject of Federal Court proceedings, alleging that Santos' statements are misleading or deceptive. Contrary to the representations made by Santos that blue hydrogen is a clean technology, it is a technology that is marred in controversy.

29. First and foremost, the claim that CCS is "low emissions" or carbon-neutral is robustly contested. A 2021 study found that the greenhouse gas footprint for blue hydrogen was more than 20% greater than burning natural gas or coal for heat,[30] without even factoring in methane emissions associated with producing blue hydrogen or the Co2 and methane generated from the combustion of natural gas when ultimately used by the end-user. This study even adopted a generous capture efficiency of 85% - that is, that the plant has the ability to capture 85% of the Co2 emissions generated during the steam methane reforming process (SMR), being the process of using heat and pressure to convert methane in natural gas into hydrogen and Co2. Actual data from one of only 2 commercially operating blue hydrogen facilities shows a mean capture efficiency of only 78.8%, with daily rates varying from 53% to 90%. The world's largest CCS facility – the Gorgon facility in Western Australia – missed its 80% capture efficiency rate by approximately 50% during its first 5 years of operation.[31] Even the "gold standard" of capture efficiency – 90% - would mean that every tonne of blue hydrogen would still produce a ton of Co2.[32] Again, neither of these efficiency rates include capturing GHG emission from end use of the natural gas.

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[28] Although the court accepted that a reduction by Royal Dutch Shell of 45% in scope 1, 2 and 3 emissions relative to *2019 levels* was also broadly in line with the Paris Agreement,[28] and this was ultimately the order that was made.
[29] Science Based Targets Initiative (2021) SBTi Corporate Manual, at page 30.
[30] Robert W. Howarth, Mark Z. Jacobson. How green is blue hydrogen? Energy Science & Engineering, 2021; DOI: 10.1002/ese3.956.
[31] Robertson and Mousavian, Institute for Energy Economics and Financial Analysis, 'Gorgon Capture and Storage: The Sting in the Tail.' Available at: https://ieefa.org/wp-content/uploads/2022/03/Gorgon-Carbon-Capture-and-Storage_The-Sting-in-the-Tail_April-2022.pdf at page 7.
[32] https://www.forbes.com/sites/jamesmorris/2021/09/25/is-carbon-capture-another-fossil-fuel-industry-con/?sh=70aef7e65ef3

30. Second, the cost of blue hydrogen production and CCS has made it commercially unviable - currently the costs remain higher than US 50tCo2. [33] The cost of just the Co2 injection system for the Gorgon CCS facility was $3.1 billion to the mid-2020s, without including the cost to capture the Co2 itself.[34] As noted above, there are currently only 2 commercial blue hydrogen plants, and neither of these plants capture the Co2 produced from burning the natural gas in the SMR process.[35] Expanding out more broadly to all CCS facilities, the 28 existing facilities capture only 0.1% of Co2 emissions annually.[36] Of that 0.1% captured, the vast majority is captured to produce more fossil fuels (a process known as Carbon Capture and Use, or CCU). Even "pure" CCS has significant geological and engineering limitations.[37]

31. Given these significant issues with CCS, it is deeply concerning that in assessing Santos' decarbonisation approach, Unisuper has assessed Santos' *"demonstrating some progress with carbon capture and storage"*[38] to be aligned with a broader decarbonisation strategy. In fact, Unisuper itself recognises that CCS as a mitigation strategy for the Barossa expansion project is a technology *"yet to be proven in the field at scale."*[39] It is inconsistent and even potentially misleading for Unisuper to recognise these issues with CCS/blue hydrogen and yet still accept them as tenable emissions reductions/emission mitigation pathways.

<u>Santos' capital allocation to new gas projects is not Paris-aligned</u>

32. When assessing Santos for alignment with the Paris Agreement, Climate Action 100 found that, as at 31 December 2021, <u>Santos failed to meet any of its criteria</u> in relation to capital allocation, being that the company is working to decarbonise its capital expenditures and that the company discloses the methodology used to determine the Paris alignment of its future capital expenditures.

33. Since December 2021 Santos has released a new capital allocation strategy. This strategy involves investing US$1.9 billion to $3.8 billion in hydrogen and ammonia hubs. Santos alleges that this investment is in line with the required level of investment in hydrogen and hydrogen-based fuels under the IEA Sustainable Development Scenario (SDS) and the NZE, being 3.7% under the SDS and 4.8% under the NZE. On this basis, Santos argues that its new capital allocation strategy is "Paris-aligned."

34. Santos' representation that their capital allocation is "Paris-aligned" is flawed and potentially misleading because it:

    a. fails to take into account the quantum or proportion of committed and sustaining capital to new oil and gas projects relative to investment in so-called "clean energy"; and

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[33] Intergovernmental Panel on Climate Change (IPPC), Climate Change 2022 Mitigation of Climate Change (Report) WG111 at 6-38. <https://report.ipcc.ch/ar6wg3/pdf/IPCC_AR6_WGIII_FinalDraft_FullReport.pdf>.

[34] https://www.smh.com.au/environment/climate-change/chevron-s-five-years-of-gorgon-carbon-storage-failure-could-cost-230-million-20211110-p597uf.html

[35] Robertson and Mousavia, at 1677,

[36] Centre for International Environmental Law (CIEL), 2021, 'Confronting the myth of carbon-free fossil fuels: Why carbon capture is not a climate solution.' Available at: https://www.ciel.org/wp-content/uploads/2021/07/Confronting-the-Myth-of-Carbon-Free-Fossil-Fuels.pdf

[37] IPCC WGIII report, Chapter 6, at 6-36.

[38] See page 5 of Unisuper's latest Responsible Investment Report.

[39] See page 6 of Unisuper's latest Responsible Investment Report.

b. relies on blue hydrogen and CCU/CCS – technologies whose net zero credentials are currently being legally challenged.

35. Climate Analytics' analysis shows that to be in line with the NZE, Australia's LNG exports will need to fall 25% below 2020 levels by 2030, and by 50% by 2035.[40] To be aligned with the IPCC's P1 and P2 1.5°C warming scenarios, global oil and gas production must fall by 30% from 2020 to 2030, and by 54% by 2040.[41] However, rather than moving to decarbonise and reduce production, Santos is ramping up oil and gas production and making major capital investment into new oil and gas projects with total capex costs reaching over US$10 billion.[42] It is estimated that between 2020 and 2027, Santos and Oil Search's annual oil and gas production will increase by over 17%. We set out how Santos is ramping up its production of oil and gas in paragraphs 40 to 42. This increase production will lead to increases in emissions over the next 5 to 10 years, with Santos' annual emissions from 2026 to 2029 estimated to be more than 25% above a combined Santos and Oil Search 2020 baseline.

36. In addition to the above, Santos' capital allocation strategies relies heavily on blue hydrogen and CCU and CCS technology. As noted in paragraphs 28 to 29 above, there are serious concerns that such technologies are not, in fact, net-zero or carbon neutral.

Issue 3: Unisuper voting against shareholder proposals in relation to effective net zero strategies

37. Whilst publicly stating that *"we continue to regularly support shareholder resolutions asking for TCFD reporting or targets where companies are not reporting or acting to decarbonise their business"* [43]and that *"the totality of our actions will be consistent with the ultimate goals of the Paris Agreement"* [44](our emphasis), Unisuper:

    a. did not vote in favour of any ESG resolutions proposed at Australian companies in 2017 to 2020[45];

    b. voted against two of Market Forces' Capital Protection resolutions proposed in 2021 and 2022 seeking that Santos disclose how its capital expenditure, operations and capital allocation are NZE and Paris-aligned;

    c. voted in favour of Santos' Climate Report which set out Santos' emission reduction commitments and transition plan notwithstanding that:

        i. Santos' plan (as set out in its Climate Report) is not Paris-aligned for the reasons set out in paragraph 18 to 36 above and paragraphs 40 to 42 below; and

        ii. Santos is scaling up oil and gas production.

    In its latest Responsible Investment Report, Unisuper stated that it supported the resolution approving the Climate Report because Santos had *"demonstrated some*

[40] https://climateanalytics.org/media/gas_is_new_coal_nov_2021_1_1.pdf
[41] https://productiongap.org/wp-content/uploads/2021/11/PGR2021_web_rev.pdf
[42] https://www.santos.com/wp-content/uploads/2021/11/211111-Oil-Search-and-Santos-merger-update-Court-approves-distribution-of-Scheme-Booklet-and-convening-of-Scheme-Meeting.pdf
[43] Page 36, Unisuper's Climate risk and Investment report August 2021.
[44] Page 3, Unisuper's Climate risk and Investment report August 2021.
[45] Australian Centre for Corporate Responsibility (ACCR), 2021, 'Super Votes: How Australia's Largest Superannuation Funds voted on ESG Resolutions in 2020.' Available at: https://www.accr.org.au/downloads/accr-supervotes-202109-final-5.pdf at page 33.

progress with Carbon Capture and Storage (CCS) technology,"[46] including as part of the Barrossa Project notwithstanding:

i. the substantive criticism of CCS (discussed at paragraphs 28 to 31 above), and the fact that Santos' reliance on such technologies is currently the subject of a Federal Court challenge; and

ii. the fact that Unisuper itself acknowledges that Co2 emissions from Barrossa will be significant, higher than other fields, and even higher than Woodside's Scarborough project.[47] The Barossa project is a new gas project that will extend for 15 - 29 years and is estimated to release 15.45 million tonnes of carbon dioxide annually. The NZE is equivocal that to achieve net zero by 2050, no new gas fields projects should be approved for development beyond those that were already committed as of 2021. It is unclear to us how Unisuper can say that the increase of Co2 emissions and expansion of fossil fuel capability is NZE or Paris-aligned; and

d. adopted wholly contradictory positions by voting 'for' a shareholder resolution on climate-related lobbying and decommissioning on the apparent basis that it believed that Santos should <u>not</u> be *"lobbying for new projects until (or unless) they can provide detailed justification as to how they are Paris-aligned"*[48] (which therefore implies that Santos is not currently Paris-aligned), whilst at the same time voting 'against' a resolution requiring Santos implement a science-based net zero target because Unisuper believed that Santos had *"already set a science-based net zero target that is aligned with the objectives of the Paris Agreement."* [49]

38. We consider that by voting in the way set out above, Unisuper is potentially in breach of its Trustee Obligations and Director Obligations. We also consider that such conduct is inconsistent with its representations, which potentially amounts misleading and deceptive conduct.

<u>Issue 4:</u> Unisuper's failure to divest from Santos

39. Our client is of the view that Unisuper's failure to divest from Santos could amount to a Trustee Breach and/or Director Breach in circumstances where:

a. Santos is scaling up oil and gas production leading to increased GHG emissions thereby exacerbating climate change and its impacts; and

b. continued investment in Santos is an investment in stranded assets that could lead to negative member financial returns.

<u>Santos' scaling up of gas production</u>

40. Rather than decreasing its greenhouse gas emissions as required under its net zero plan, analysis of Santos' 2021 Climate Change Report by the Institute for Energy Economics and Financial Analysis reveals that Santos' total (Scope 1, 2 and 3) emissions rose by 53% in 2020-21, and by 94% since 2016-2017. [50]

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[46] See Pages 5 and 6 of Unisuper's Responsible Investment Report 2022.
[47] Pages 5 and 6 of the Responsible Investment Report 2022.
[48] Page 6 of the Responsible Investment Report 2022.
[49] Ibid.
[50] IEEFA, 'Santos 2022 Climate Change Report- A Reality Check', https://ieefa.org/wp-content/uploads/2022/04/Santos-2022-Climate-Change-Report-A-Reality-Check_April-2022.pdf

41. As the holder of the largest number of offshore exploration permits, and the largest offshore area under exploration,[51] Santos has announced that it will be spending US$1.15billion - $1.3billion on new oil and gas projects,[52] including, relevantly:

a. **Narrabri Gas coal seam gas project in northern New South Wales**, whereby Santos could extract up to 200 terajoules (TJ) of gas per day over 20 years through unconventional gas extraction.[53] If combusted, 200 TJ of gas would release 10,000 tonnes of CO2-e. On top of this, experts have highlighted the project's significant potential impacts on Aboriginal cultural heritage, groundwater, and local bush and farmland.

b. **Barossa Gas Project**, being an offshore gas project being progressed by Barossa Joint Venture comprising Santos as the operator (and 62.5% stakeholder in joint venture). The Barossa is a new source of gas that will extend for 15-20 years some 300km offshore from Darwin, near the Tiwi Islands. It is estimated that the project when extracted, developed and burned would release 16.5 million tonnes of carbon dioxide annually.[54] The project is currently the subject of a challenge by Tiwi Islander Elder on the basis of lack of consultation with the relevant Traditional Owners.[55]

c. **Beetaloo Basin projects**, where Santos is currently undertaking exploration activities in the Beetaloo Basin with a view to seeking further approvals to conduct commercial production in the area. It has been involved in disputes with pastoralists and traditional owners over the shale fracking operation that have delayed some of the exploration.[56]

d. **Derado oil project,** off the coast of WA is estimated to produce up to 350 barrels of oil over 20 years from 2024 amounting to an estimated 165 million tonnes of Co2 (equivalent to 46 years of operation of the Muja power station in WA)[57]. According to Carbon Tracker, this project is incompatible with even the IEA's net-zero by 2070-aligned Sustainable Development Scenario (SDS), let alone the far more constrained demand profile imposed by the NZE.[58]

42. According to Market Forces, on a conservative estimate, Santos' increasing oil and gas production plans would lead to an over 20% increase in annual emissions to 2029 above a 2020 baseline that combines Santos and Oil Search production that year.[59]

Stranded assets likely to cause negative member returns

43. As the world de-carbonises, there is a real and foreseeable, and potentially substantial, risk that investment in gas projects is investment in "stranded capital." The IEA defines "stranded capital" as investment in fossil fuel infrastructure that is not recovered over the operating lifetime of the asset because of reduced demand or reduced prices resulting from climate

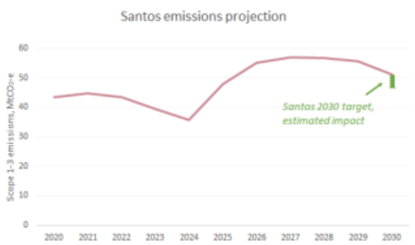
[51]Ibid at page 2
[52]Ibid at page 1.
[53] NS Energy, 'Narrabri Gas Project', https://www.nsenergybusiness.com/projects/narrabri-gas-project/
[54] See www.stopbarossagas.org
[55] See https://www.edo.org.au/tiwi-islands-barossa-gas-drilling-challenge/
[56] See https://ntindependent.com.au/santos-agrees-to-pay-400k-to-rallen-over-beetaloo-basin-gas-wells/
[57] https://www.boilingcold.com.au/santos-oil-dorado-is-a-lode-of-scope-3-emissions/
[58] https://www.marketforces.org.au/wp-content/uploads/2022/03/2022-03-STO-WPL-investor-briefing.pdf at page 6.
[59] noting merger between the two companies was implemented on 17 December 2021. See https://www.marketforces.org.au/investor-demands-for-santos-to-wind-down-oil-and-gas-production-increase-to-15/

policies.[60] This then prompts a reduction in the value of equity in gas companies such as Santos in circumstances where future revenue generated by these companies is reduced.[61]

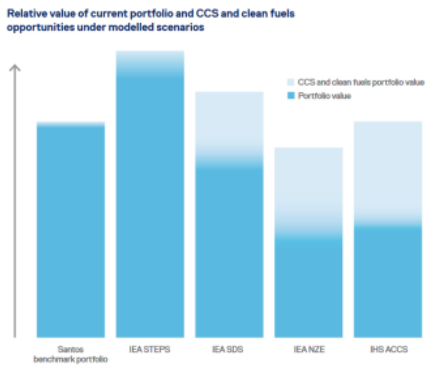
44. According to the NZE, supply of natural gas is estimated to peak in the mid-2020s, and thereafter continue to fall, with an annual average decline of just under 3% from 2020 to 2050,[62] with natural gas use 55% lower in 2050 than in 2020.[63] As a result of the reduction in use and demand, the IEA estimates that between 2020 and 2050 natural gas traded as LNG will fall by 60% and trade by pipeline will fall by 65%, with declines of more than 4% per year on average during the 2030s, causing some gas fields to be closed prematurely. As a result, the IEA states that no new natural gas fields or LNG facilities need to be approved or built beyond that which is already approved as of 2021.[64] This message is reinforced by analysis undertaken by Wood Mackenzie on behalf of the IGCC, in which Wood Mackenzie concludes that:

> *"Under the 1.5°C scenarios explored in this report, Australian gas will have a diminishing role in the transition to net-zero emissions, particularly from the 2030s onwards. By 2050, Australia is forecast to have minimal LNG exports or domestic gas demand, suggesting new projects carry a substantial risk of stranding should key policy and market changes materialise".*[65]

45. Santos' Climate Change report shows that Santos itself predicts that the value of its oil and gas portfolio would drop by around 50% under the IEA's Net Zero by 2050 pathway (see charts below).



Source: Market Forces analysis of Grant Samuel Independent Expert's Report, contained in Santos and Oil Search merger Scheme Booklet; 2022 Climate Change Report



Source: Santos 2022 Climate Change Report, pg 40

<u>Unisuper's position on divestment is contradictory</u>

46. Unisuper seems to have contradictory statements about divestment from fossil fuels. Whilst its Climate Change Position Statement states that Unisuper states that "*divestment of ownership, while always an option, will reduce the influence we have over companies"* and that *"the greatest impact we have is owning stakes in companies. Ownership provides us with scope to directly influence companies through engagement or exercise our voting rights"*

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[60] IEA (2021) net zero by 2050 A Roadmap for the Global Energy Sector, First Edition, May 2021 at page 102.
[61] IEA (2021) net zero by 2050 A Roadmap for the Global Energy Sector, First Edition, May 2021 at page 102.
[62] Ibid at page 57.
[63] Ibid at page 101.
[64] Ibid at 1102 – 103.
[65] Investor Group on Climate Change (IGCC), 2022, 'Changing pathways for Australian gas: A 1.5°C scenario analysis of new Australian gas projects,' Available at: https://igcc.org.au/wp-content/uploads/2022/04/IGCC-Changing-pathways-for-Australian-gas-FINAL.pdf at page 13.

(**Divestment Position**), it also (in the same document) states that *"a prudent approach to portfolio management will involve the avoidance of assets that are most likely to be stranded"* and that *"ultimately, in circumstances when we believe that the strategy of a company is not aligned with our long-term aims, we have the option of divesting."*

47. The Divestment Position is inconsistent with Unisuper's actions in the following respects:

    a. Unisuper's history of voting on shareholder resolutions as part of its "engagement" strategy is not consistent with Paris-alignment for the reasons set out in paragraphs 37 and 38 above;

    b. contrary to its Divestment Position, Unisuper has nevertheless sought to de-carbonise its investments, having reported that it reduced its fossil fuel exposure across the fund from 2.55% down from 5.05%, that it has divested from companies that generate greater than 10% of their revenue from the extraction of thermal coal, and that it is in the process of incorporating an effective cap on fossil fuel exposure. Such divestment actions are contradictory to its Divestment Position; and

    c. it is unclear how continued investment in Santos follows Unisuper's strategy of the "avoidance of assets that are most likely to be stranded" and how Santos' core business of oil and gas exploration and increasing production could be Paris-aligned and therefore aligned with Unisuper's long-term aims.

48. In light of the above and the long-term horizon over which super trustees invest member funds, there is a real risk that continuing to invest in Santos' equities may amount to a breach of Trustee and Director Duties.

Misleading or deceptive conduct

49. Our client is concerned that the representations set out in **Annexure A**, alone or in combination convey that:

    a. Unisuper is a leader on climate action;

    b. Unisuper's corporate and investment strategy are aligned with the Paris Agreement;

    c. Unisuper is reducing its portfolio emissions and aims to reach net zero by 2050;

    d. Unisuper's investment strategy (including its consideration of climate) will help deliver long-term value for Unisuper members;

    e. Unisuper is committed to reducing its environmental impact; and

    f. Unisuper has been engaging with those companies in which it is invested (including Santos) to transition them in line with the Paris Agreement.

    (collectively, the **Representations**).

50. The Representations are misleading or deceptive or likely to mislead or deceive members or potential members for the reasons set out in paragraphs 18 to 45 above, being (in summary):

    a. Unisuper continues to invest in Santos, which is a major contributor to global warming;

    b. Santos' net zero pathway does not involve a Paris-aligned reduction in scope 3 emissions;

c. Santos' net zero representations are dependent on CCS and blue hydrogen; and

d. notwithstanding their apparent net zero representations, Santos has plans to scale up and/or expand its fossil fuel projects, leading to increased emissions. Such actions are contrary to the IEA's statements under the NZE that to achieve net zero by 2050 no new oil or gas fields could be approved for development from 2021.[66]

Requested action

51. In light of the above, our client considers that the appropriate way in which Unisuper can avoid these significant liability risks arising as a result of potential breach of Trustee Duties, Director Duties and misleading or deceptive conduct, is to **divest from Santos.**

52. As interim steps, our client requests that no later than **COB on 16 September 2022**, pursuant to s 1017C of the Corporations Act, Unisuper provides our client with the following information, being information that our client reasonably requires for the purposes of making an informed judgment about the management and the financial condition of the superannuation entity:

    a. a substantive response to the issues set out in this letter, including, namely:

        i. the basis on which Unisuper considers that continued investment in Santos (in light of the issues raised in this letter) is not a breach of Trustee and Director duties; and

        ii. the basis on which Unisuper makes the Representations.

53. Our client reserves her rights to take further action in respect (but not limited to) the issues set out in this letter, including, potentially raising these issues with relevant regulators and/or considering other possible actions such as commencing proceedings.

Yours faithfully,

Environmental Defenders Office

Kirsty Ruddock
Managing Lawyer
Safe Climate (Corporate & Commercial)

Anna Gudkov
Senior Solicitor
Safe Climate (Corporate & Commercial)

[66] International Energy Agency, 2021, 'Net Zero by 2050 A Roadmap for the Global Energy Sector. International Energy Agency,' Available at: https://www.iea.org/reports/net-zero-by-2050

Annexure A: Unisuper representations

Responsible Investment Report Jan – June 2022

- That Santos' decarbonisation approach included "net zero scope 1, 2, and 3 by 2040".

Annual Report 2021

- *"In October 2020, Unisuper made the important step of committing to net zero carbon emissions for our investment portfolios by 2050, in alignment with the Paris Agreement."*
- *"Unisuper aims to be at the forefront of the superannuation industry as it transitions to a low carbon world"*

Climate risk and our investments – August 2021

- *"The Paris Agreement of 2015 committed its signatories to a set of actions that would limit the rise in temperature to well below 2 degrees Celsius above pre-industrial levels by the second half of the century. Accordingly, we fully support the Paris Agreement and intend to play our part in ensuring Australia fulfills its commitments as a signatory"*
- *"The totality of our actions will be consistent with the ultimate goals of the Paris Agreement"*
- *"By 2050, we fully expect that all economies and companies operating in the world will have achieved net-zero emissions. Accordingly, having a net-zero portfolio will not place undue constraints on our investment universe."*
- *"We'll contribute a 45% reduction in Australia's emissions by 2030 through company engagement, advocacy and investing capital in companies needed to achieve a net-zero future"*
- *"We expect that all portfolio investments …proactively mitigate and manage climate change risks in their business and supply chains"*
- *"our ability to vote on company resolution is reinforced by direct and regular engagement with company management and boards to support a Paris-aligned decarbonization transition."*
- *"In relation to climate change, our expectation of Portfolio Companies include…a proactive approach to reducing emissions aligned with the Paris Agreement"*
- *"Engaging with our portfolio companies is our primary strategy for addressing climate-related risks"*
- *"We continue to regularly support shareholder resolutions asking for TCFD reporting or targets where companies are not reporting or acting to decarbonize their business"*

Climate Change position statement

- *"In line with our status as a leading superannuation fund, UniSuper aims to be at the forefront of the industry in transitioning to a low carbon world"*
- *"The Paris Agreement of 2015 committed its signatories to a set of actions that would limit the rise in temperature to well below two degrees above pre-industrial levels by the second half of the century. Accordingly, UniSuper is fully supportive of the Paris Agreement and intends to play its part in ensuring that Australia fulfills its commitments as a signatory."*
- *"A prudent approach to portfolio management will involve the avoidance of assets that are most likely to be stranded."*
- *"We are aiming for 100% of Australian companies held in our actively managed portfolios to have publicly stated Paris-aligned commitments by the end of 2021. As a first step we want*

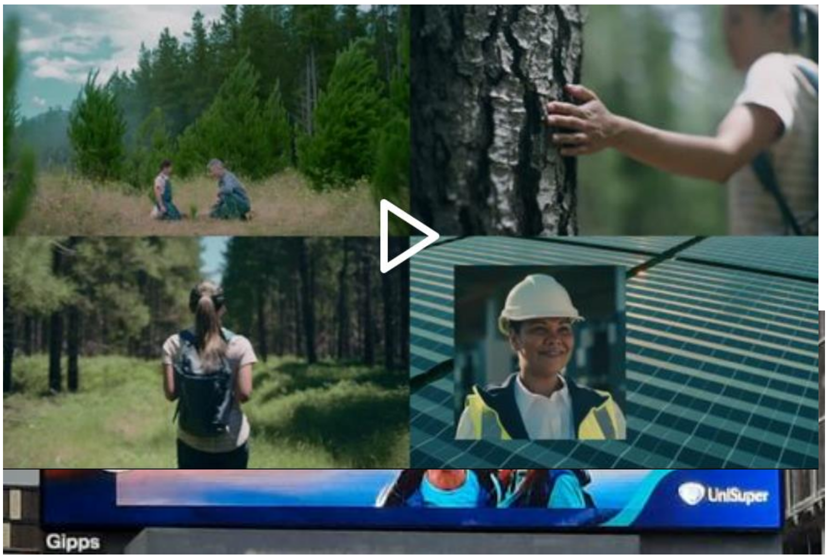
companies to disclose emission footprint and targets in a manner consistent with the framework designed by the Taskforce for Climate-related Financial Disclosures (TCFD).”

- *“The UniSuper Board and Management believe that the above set of commitments places the fund as one of the leaders in demonstrating alignment with the ultimate goal of the Paris Agreement.”*

<u>Website</u>

- *“UniSuper is committed to achieving net zero absolute carbon emissions in our investment portfolio by 2050, in alignment with the Paris Agreement.”*
- *“As Australia’s fund for the higher education sector, aligning with the Paris Agreement reinforces our long-held commitment to incorporate environmental, social and governance (ESG) factors into all investment decisions.”*
- *“In line with our status as a leading fund, we aim to be at the forefront of the transition to a low-carbon world”*

<u>Unisuper advertising</u>



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