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The evolving ESG legislative landscape 20 April 2023

David Ballegeer, Tom Cobbaert and Guillaume Croisant



Environmental, Social and Governance

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Context







Final Report 2018 by the High-Level Expert Group on Sustainable Finance Secretariat provided by the European Commission



- >Binding EU Climate Law
- >Disclosure to foster private investment needed for the transition
- >Evolving towards binding commitments and net-zero plans

EU mandatory disclosure obligations and due diligence

Corporate Sustainability Reporting Directive **Taxonomy** (CSRD) Regulation Art. 8 KPIs for corporates and financial undertakings and Green Sustainable **Asset Ratio Financial** Disclosure Regulation (SFDR - FMP)

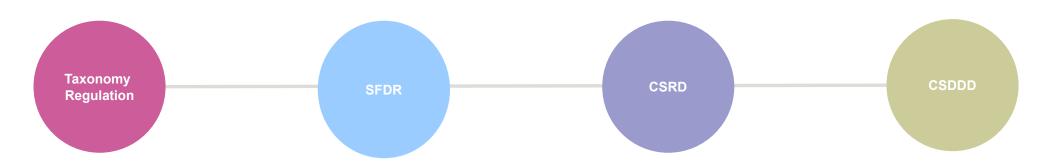
Increased granular disclosure

- > Re-direct private investment to finance net-zero transition
- > Consistency & comparability
- > Reliability



Corporate Sustainability Due Diligence Directive (CSDDD)

EU mandatory disclosure obligations and due diligence



- > Provides a means to determine which economic activities are "environmentally sustainable".
- > Puts forward reporting requirements on Taxonomy-eligibility in a first instance and Taxonomy-alignment thereafter (specific KPIs).

> Lays down rules on transparency with regard to the integration of sustainability risks and the consideration of adverse sustainability impacts in processes and the provision of sustainability-related information with respect to financial products.

- > Requires disclosure of ESG risks and impacts in line with specific mandatory EU sustainability standards.
- > Requirement for limited assurance.

- > Lays down due diligence obligations for in-scope EU and non-EU entities in relation to human rights and environmental impacts.
- > Council position published in December 2022. Further changes are expected before the regime is finalised.

Taxonomy Regulation

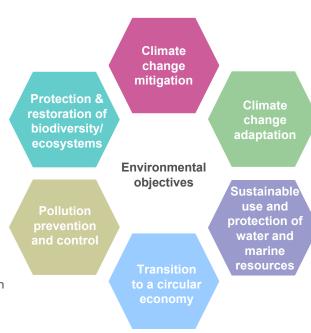
The Taxonomy Regulation provides a means to determine which economic activities are "environmentally sustainable". Only some economic activities can qualify for Taxonomy-alignment.

To qualify as "environmentally sustainable" an economic activity must:

- substantially contribute to one of six objectives (detailed technical screening criteria apply)
- do no significant harm to the objectives (detailed technical screening criteria apply)
- 3 be carried out in accordance with minimum social and governance safeguards

The Taxonomy Regulation puts forward reporting requirements:

- > non-financial undertakings have to report on their turnover, capital expenditures and operating expenditures
- > financial undertakings, which include banks, asset managers, investment firms and insurers/reinsurers, have to report on specific KPIs



Non-Financial Reporting Directive

evolving to Corporate Sustainability Reporting Directive

Scope: from public-interest entities with more than 500 employees currently to all large EU entities and certain large non-EU entities as from 2025/2026 (FY24/25), certain EU and non-EU SMEs as from 2027 (FY2026) and certain non-

EU groups as from 2029 (FY 2028)

Report on:

- Environment,
- · Social and employees,
- Respect for human rights, and
- Bribery and corruption

to the extent necessary for understanding of the company's development and performance Report on full range of ESG issues relevant to the business, with double materiality:

- 1) risks to the company arising from sustainability issues; and
- 2) company's impact on people and the environment

Auditor limited assurances

Net-zero transition plan in line with 1.5°C Paris Agreement

Information on companies' global supply chain and human rights due diligence under Sustainable Corporate Governance

European Sustainability Reporting Standard (ESRS) prepared by EFRAG

Corporate Sustainability Reporting Directive (CSRD)

Under the CSRD, specified EU and non-EU undertakings will need to disclose on an annual basis information necessary to understand the undertaking's / group's impacts on sustainability matters and how sustainability matters affect the undertaking's / group's development, performance and position.

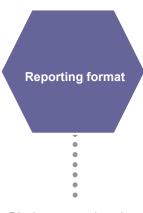


Disclosure required across broad range of factors (see list on the right)

Disclosures must be in line with specific EU sustainability standards



Undertakings must ensure reported sustainability information is subject to (limited) assurance



Disclosure needs to be included in management reports

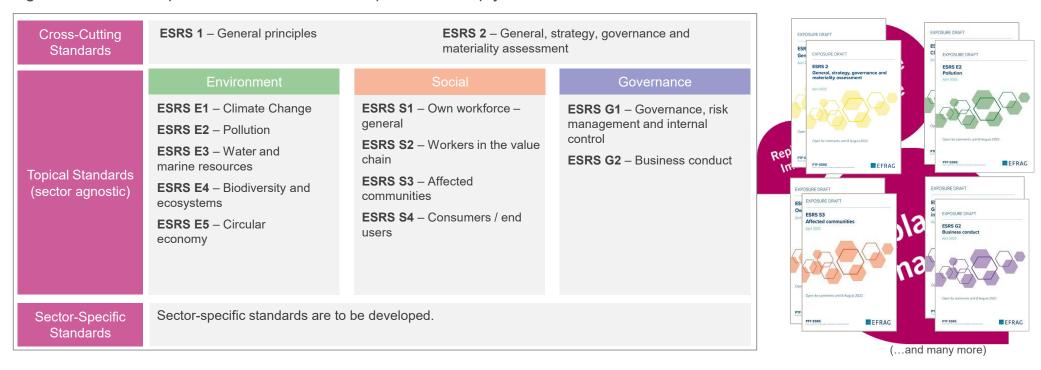
Undertakings also have to digitally 'tag' the reported information, so it is machine readable

CSRD disclosures must describe:

- the undertaking's / group's business model and strategy, including:
 - > the **resilience** of the model and strategy to risks related to sustainability matters;
 - > **opportunities** relating to sustainability matters;
 - > climate transition plan (in line with 1.5C warming); and
 - > how stakeholder interests and sustainability impacts of the business are taken into account;
 - how the undertaking's / group's strategy has been implemented with regard to sustainability matters;
- > the undertaking's / group's **targets** related to sustainability matters and progress against them;
- > the role of admin, management and supervisory bodies with regard to sustainability matters;
- > policies relating to sustainability matters; and
- > the **due diligence process** implemented with regard to sustainability matters;
 - actual/potential impacts connected to the undertaking's / group's value chain;
 - actions taken to prevent, mitigation or remediate impacts; and
 - > **principal risks** to the undertaking related to sustainability matters incl. dependencies, and how these are managed.

European Sustainability Reporting Standards (ESRS)

The European Financial Reporting Advisory Group (EFRAG) has developed detailed Sustainability Reporting Standards which organisations in scope of the CSRD will be required to comply with.



Transition plans under ESRS E1

The undertaking shall disclose its transition plan for climate change mitigation

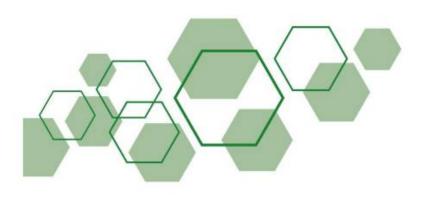
"The plans and capacity of the undertaking to adapt its business model(s) and operations in line with the transition to a sustainable economy and to contribute to limiting global warming to 1.5°C"

Granular disclosure, including scope 1 (own production), scope 2 (energy) and scope 3 (up- and downstream value chain)

- → internal governance processes and policies
- → improving transparency and sustainability in the supply chain
- → third-party certification

DRAFT EUROPEAN SUSTAINABILITY REPORTING STANDARDS

ESRS E1 Climate change



November 2022



Key takeaways



Comprehensive set of mandatory sustainable reporting under European Sustainability Reporting Standards (ESRS)



Double materiality in EU (different from other standards)



Net-zero transition plan commensurate with 1.5°C target, resilience, ability to adapt



Past performance and forward-looking (short, medium & long-term)



Dynamic nature of climate-risk reporting → impact on materiality?



Auditor vetting; regulatory supervision



Data, data & data

Proposal for a Corporate Sustainability Due Diligence Directive (CSDDD)

Due diligence

> companies covered by the Proposal must conduct human rights and environmental due diligence (based on existing international soft law standards e.g. the OECD Due Diligence Guidance for Responsible Business Conduct, the UN Guiding Principles on Business and Human Rights and the OECD Guidelines for Multinational Enterprises).

Climate change transition plan

- > In-scope companies (with limited exceptions) must adopt a plan ensuring their business model and strategy are compatible with a transition to a sustainable economy, including limiting global warming to 1.5 °C
- > Identify the extent of risk or impact of climate change on operations and include emission reduction objectives where relevant

Directors' duties

- > Directors of in-scope **EU** companies responsible for overseeing companies' due diligence actions
- > Must take sustainability into account under duty to act in best interests of company
- EU Member States to ensure breach of above duty is considered breach of directors' duties under domestic law



CSDDD – key other supply chain regulatory initiatives (incl. in Belgium)

Dutch Child Labour Due Diligence Law and Act on responsible and sustainable international operations

Child labour-focussed due diligence obligation applicable to companies operating in the Netherlands. It is unclear if and when it is expected to come into force. Current expectation is that the Dutch Child Labour Due Diligence Law will be revoked upon adoption of the legislative proposal Act on responsible and sustainable international operations which provides for broader set of obligations and includes all core elements of the Dutch Child Labour Due Diligence Law.

Swiss Conflict Minerals regime

Due diligence and reporting obligations focussed on child labour and adverse impacts occurring in the supply chains of those importing tin, tantalum, tungsten and gold from conflict-affected and high-risk areas, imposed on all Swiss companies (where relevant). Financial penalties can apply in case of breach. Expected to come into force from 1 January 2023.

Latin America

Various countries are considering legislation. In Mexico, there are new environmental risk evaluation requirements and a legislative reform initiative is proposed which if passed would impose a corporate obligation to implement human rights risk analysis (following a failed attempt at the same in 2020). Many countries (e.g. Peru, Colombia, Chile, Brazil) have a National Action Plan in Business and Human Rights some of which include promoting implementation of due diligence processes for large companies. Various countries are looking to introduce additional protections for indigenous communities, including Mexico.

- Represents a reporting obligation
- Represents a due diligence (with reporting) obligation
- Represents a country/region where proposals for regimes are being developed/considered

Norwegian Transparency Act

Due diligence and reporting obligations covering human rights and decent work. applicable to large companies doing business in Norway. Financial penalties can apply in case of breach. Comes into force on 1 July 2022.

Belgian Duty of Vigilance Bill

Legislative proposal aiming to introduce in Belgium a regime similar to the French Duty of Vigilance Law.

EU Conflict Minerals Regulation

Due diligence and reporting obligations that cover adverse impacts occurring in the supply chains of those importing into the EU tin, tantalum, tungsten or gold from conflict-affected or high-risk jurisdictions, applicable to Union Importers based on an annual import threshold. Enforcement is Member State specific.

No legislation to directly address human rights and modern slavery. A draft modern slavery bill was tabled in Hong Kong in 2018, but has not been passed into law. In August 2022, the Japanese government published draft human rights due diligence guidelines to help companies identify and prevent human rights-related abuses in their global supply chains. The guidelines will be non-binding but legislation against human rights abuses may follow.

California Transparency in Supply Chains Act

Modern slavery-focussed reporting obligation applicable to retail manufacturers or sellers in California who meet a revenue threshold. Relies heavily on public censure

UK Modern Slavery Act

Modern slavery-focussed reporting obligation applicable to companies carrying on business in the UKwho meet a turnover threshold. Relies heavily on public censure for enforcement.

French Duty of Vigilance Law

Due diligence and reporting obligations covering human and fundamental rights, health and safety and the environment, applicable to companies operating in France based on employee headcount. Financial penalties can apply in case of breach

German Supply Chain Due Diligence Act

Due diligence and reporting obligations covering human rights and the environment applicable to companies located in Germany based on employee headcount. Financial penalties apply in case of breach. Will come into force from 2023 (3.000 staff) and 2024 (1.000 staff).

Australian Modern Slavery Act

Modern slavery-focussed reporting obligation applicable to companies registered in or carrying on business in Australia who meet a revenue threshold. Relies heavily on public censure for enforcement.



What does this mean for business?

- Ensure senior level engagement
- Know and own the commitments you have made even if these are 'voluntary'
- Build capacity and dedicate resource
- Cascade through the whole business
- Strive for continuous improvement, but expect to be judged with hindsight
- Engage, **Know your** review and risks and take walk the talk action **Identify leverage** and engage with remedy
- Develop a comprehensive due diligence strategy to understand exposures
- > Be aware of the expanded boundaries of the corporate – focus on the value chain
- > Understand double materiality and its consequences
- > Know how to test information received from counterparties (no news and too much good news are not positive indicators)

- Always have one eye on creating leverage
- Understand that remedy does not always mean financial compensation
- Treat remedy as a risk management tool not a concession

- Outreach, engagement and good listening are key to understanding human rights impacts
- > Develop and deploy effective grievance mechanisms to support information gathering

The rise of climate (and other ESG) litigation

