

Linklaters

# The evolving ESG legislative landscape

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David Ballegeer, Tom Cobbaert and Guillaume Croisant

Environmental, Social and Governance

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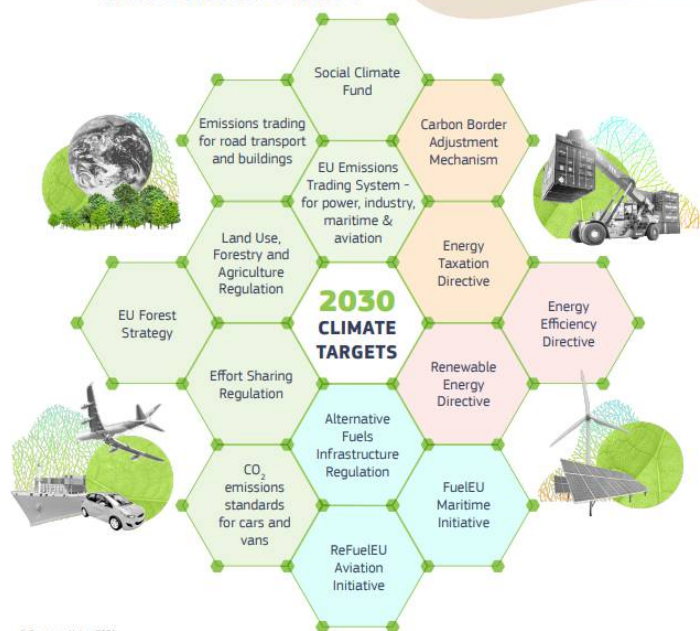


# Context

## DELIVERING THE EUROPEAN GREEN DEAL

THE DECISIVE DECADE

The EU will **reduce its net greenhouse gas emissions by at least 55% by 2030**, compared to 1990 levels, as agreed in the EU Climate Law. On 14 July 2021, the Commission presented proposals to deliver these targets and make the European Green Deal a reality.



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EU HIGH-LEVEL EXPERT GROUP ON  
SUSTAINABLE FINANCE



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

## Linklaters

# EU mandatory disclosure obligations and due diligence

Corporate  
Sustainability  
Reporting  
Directive  
(CSRD)

Sustainable  
Financial  
Disclosure  
Regulation  
(SFDR – FMP)

Taxonomy  
Regulation  
Art. 8 KPIs for  
corporates and  
financial  
undertakings  
and Green  
Asset Ratio

Increased granular disclosure

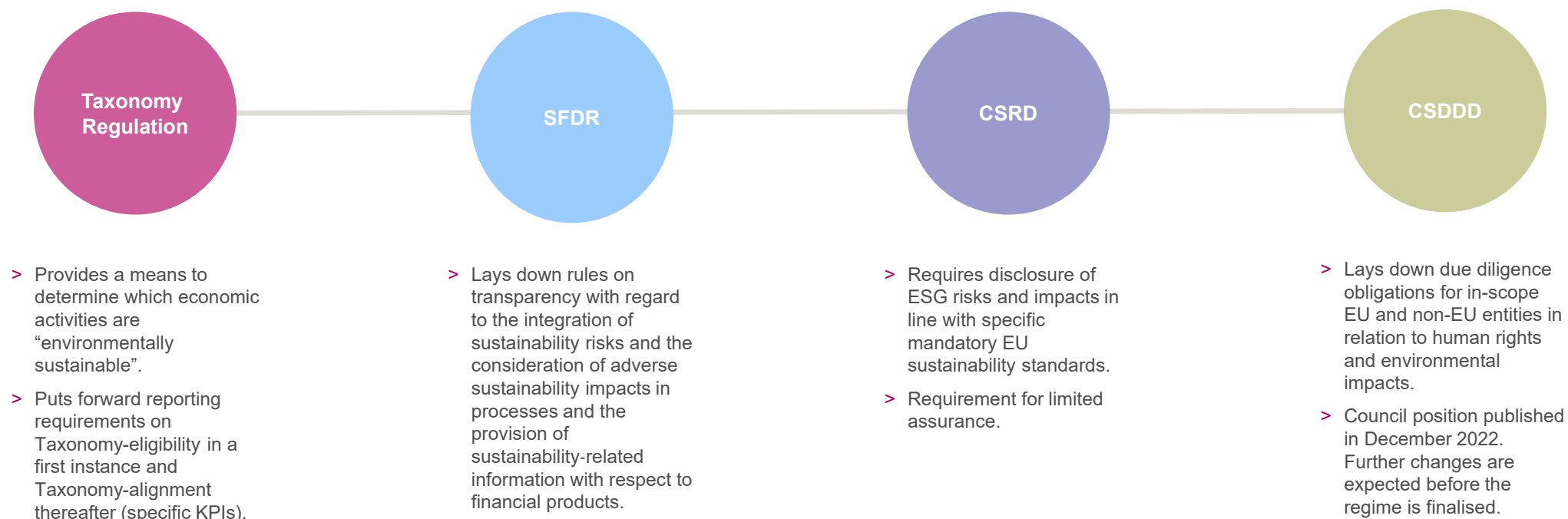
- > Re-direct private investment to finance net-zero transition
- > Consistency & comparability
- > Reliability



Corporate Sustainability Due Diligence  
Directive (CSDDD)

# EU mandatory disclosure obligations and due diligence

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# Taxonomy Regulation

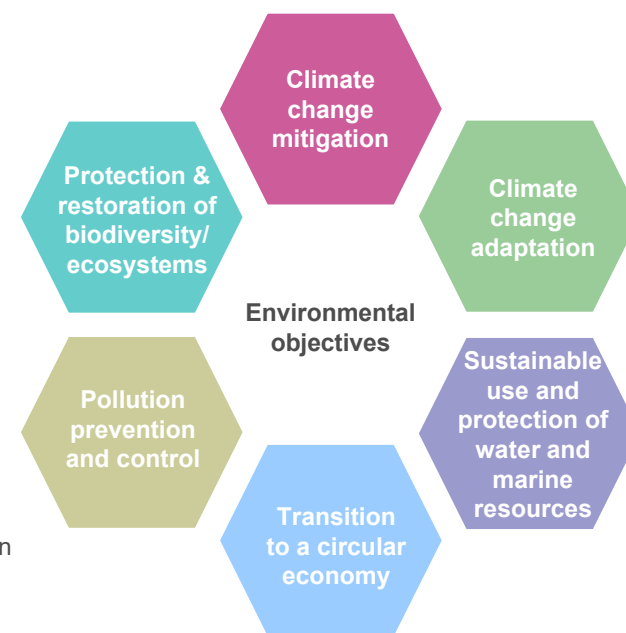
The Taxonomy Regulation provides a means to determine which economic activities are “environmentally sustainable”. Only some economic activities can qualify for Taxonomy-alignment.

To qualify as “environmentally sustainable” an economic activity must:

- 1 **substantially contribute** to one of six objectives (detailed technical screening criteria apply)
- 2 **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

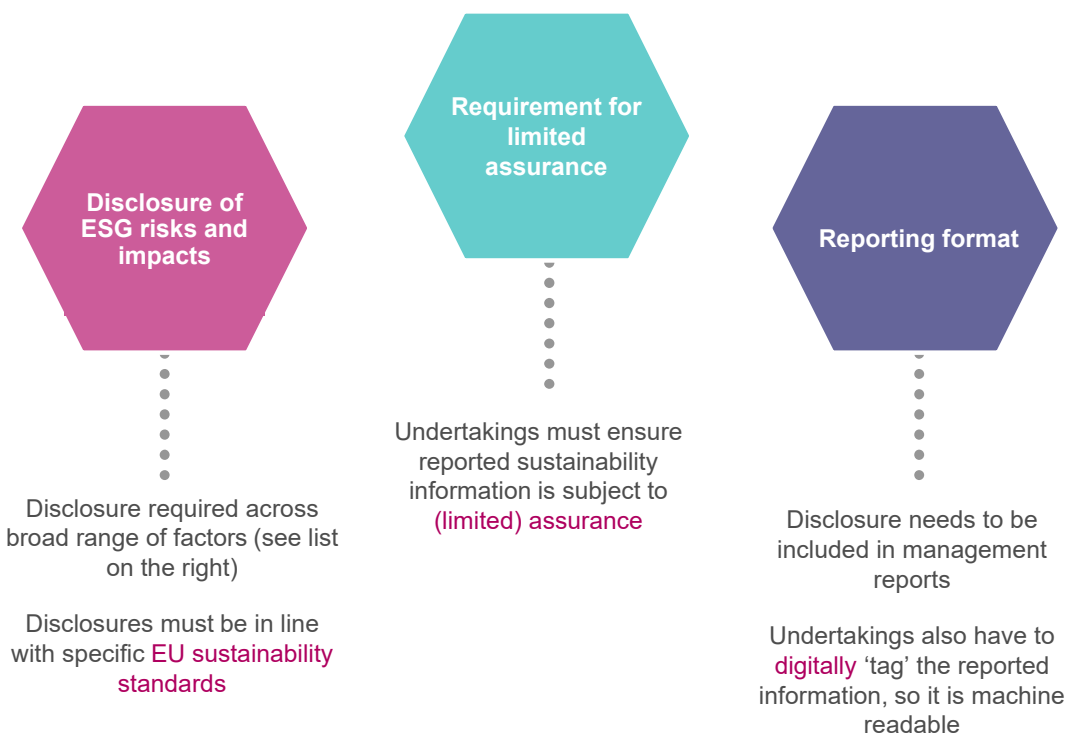
Information on companies' global supply chain and human rights due diligence under Sustainable Corporate Governance

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.



## 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.

Cross-Cutting Standards	ESRS 1 – General principles		ESRS 2 – General, strategy, governance and materiality assessment	
Topical Standards (sector agnostic)	Environment	Social	Governance	
	<div>ESRS E1 – Climate Change</div> <div>ESRS E2 – Pollution</div> <div>ESRS E3 – Water and marine resources</div> <div>ESRS E4 – Biodiversity and ecosystems</div> <div>ESRS E5 – Circular economy</div>	<div>ESRS S1 – Own workforce – general</div> <div>ESRS S2 – Workers in the value chain</div> <div>ESRS S3 – Affected communities</div> <div>ESRS S4 – Consumers / end users</div>	<div>ESRS G1 – Governance, risk management and internal control</div> <div>ESRS G2 – Business conduct</div>	
Sector-Specific Standards	Sector-specific standards are to be developed.			





## Transition plans under ESRS E1

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### **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**

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### **ESRS E1 Climate change**



November 2022

## Key takeaways

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- ✓ 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

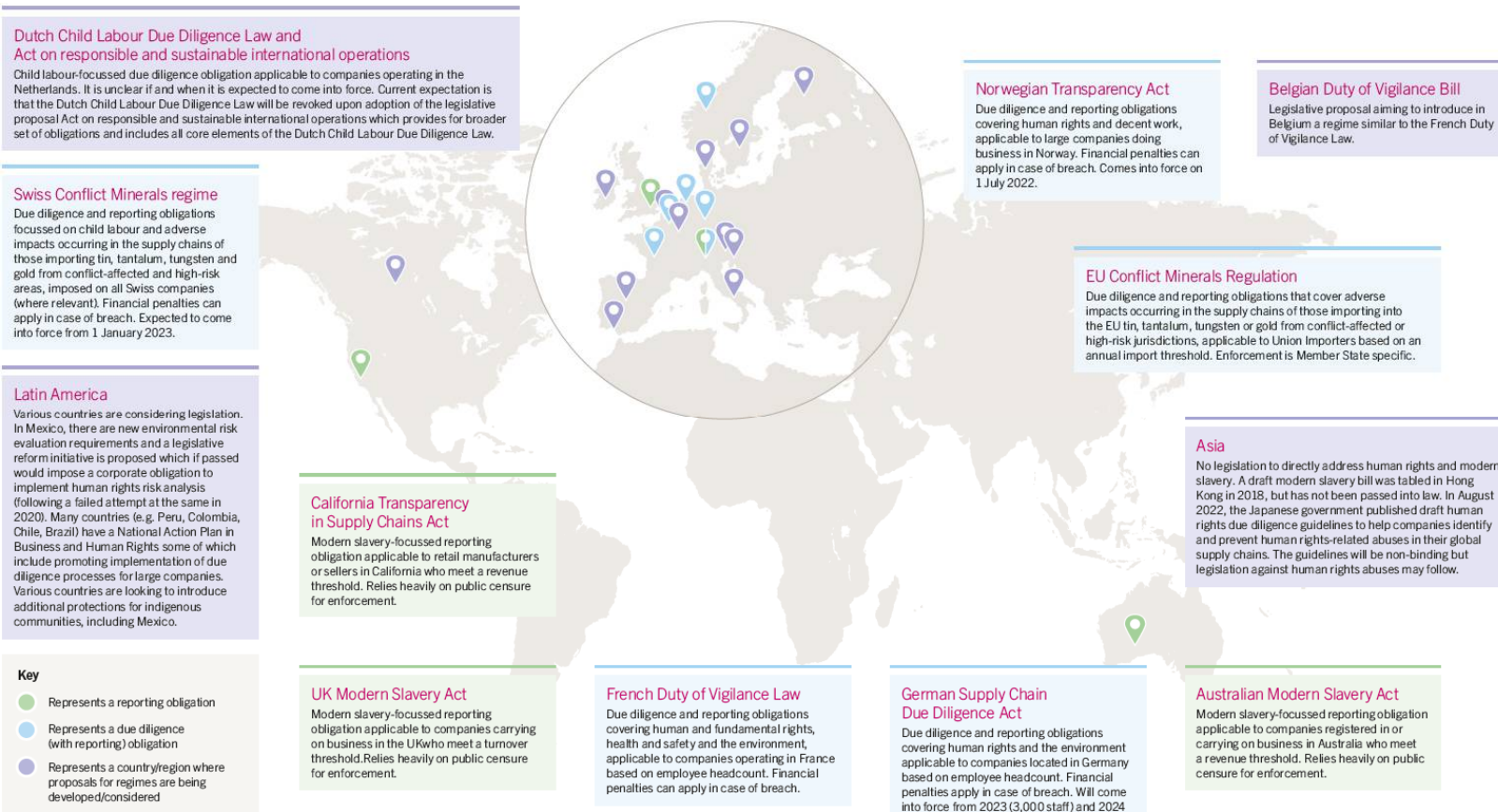
- > In-scope companies (with limited exceptions) must adopt a plan ensuring their business model and strategy are compatible with a transition to a sustainable economy, including limiting global warming to 1.5 °C
- > Identify the extent of risk or impact of climate change on operations and include emission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



# 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

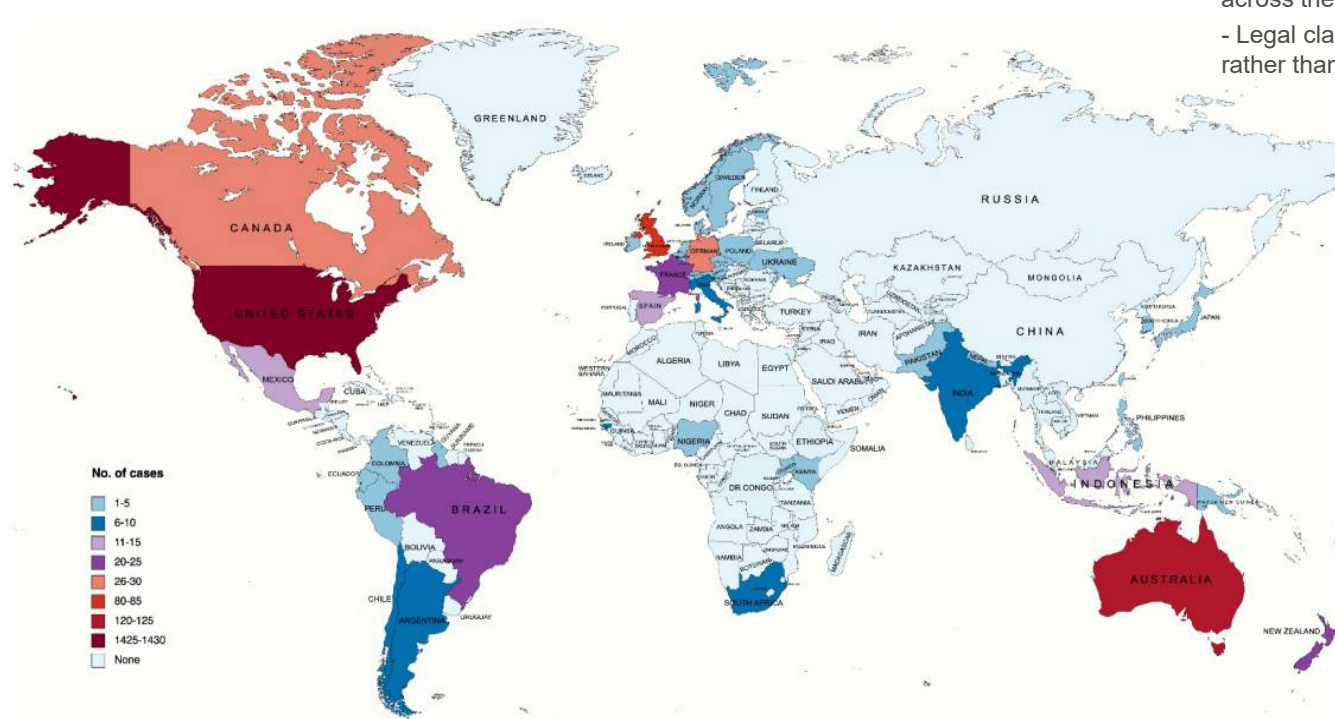
- > Always have one eye on creating leverage
- > Understand that remedy does not always mean financial compensation
- > Treat remedy as a risk management tool – not a concession



- > 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)

- > 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



- There is an increasing variety of ESG legal claim trends across the globe.
- Legal claims may be brought for strategic reasons, rather than because of anticipated success.



**Source:** LSE - Global trends in climate change litigation; cumulative figures to May 2022, Sabine Center Climate Litigation Database.



Questions

