Policy recommendations on Article 15 "Combating climate change" of the proposed EU Corporate Sustainability Due Diligence Directive

In light of the severity and the short timeframe that remains to take action to limit global warming to 1.5 degrees, it is important that the EU Corporate Sustainability Due Diligence Directive (CSDDD) leaves no legal ambiguity concerning corporate obligations regarding climate change. The aim of this paper is to provide **recommendations on Article 15** "Combating climate change" of the Commission's proposal which lacks precision regarding the targets and content of the transition plans it refers to. The **Corporate Sustainability Reporting Directive (CSRD) already provides a baseline** for coherence. CSDDD should not fall behind that baseline, in order for both legislations to support the effectiveness of one another.

These recommendations on Article 15 **need to be accompanied by changes to Article 3 of the proposed CSDDD, that would ensure a comprehensive approach to the definition of environmental adverse impacts.** The definition should not only capture the effect that companies have on all three - the environment, climate and human rights - but also how these are interdependent and what damage prevention entails.

Briefing supported by:

Why more specificity is needed in Article 15

a) Transition plans

A specification of the key elements of transition plans is crucial to ensure effective enforcement, the needed comparability among companies, and to provide legal certainty. The **criteria for transition plans should at a minimum be coherent, with the ones defined in the CSRD** and the EU draft reporting standards proposed by EFRAG.[1]

Article 15 should include a clear requirement for all companies within the scope of the CSDDD to implement transition plans and establish content criteria, based on the ones developed under the CSRD and the draft EU reporting standards. In particular, transition plans should:

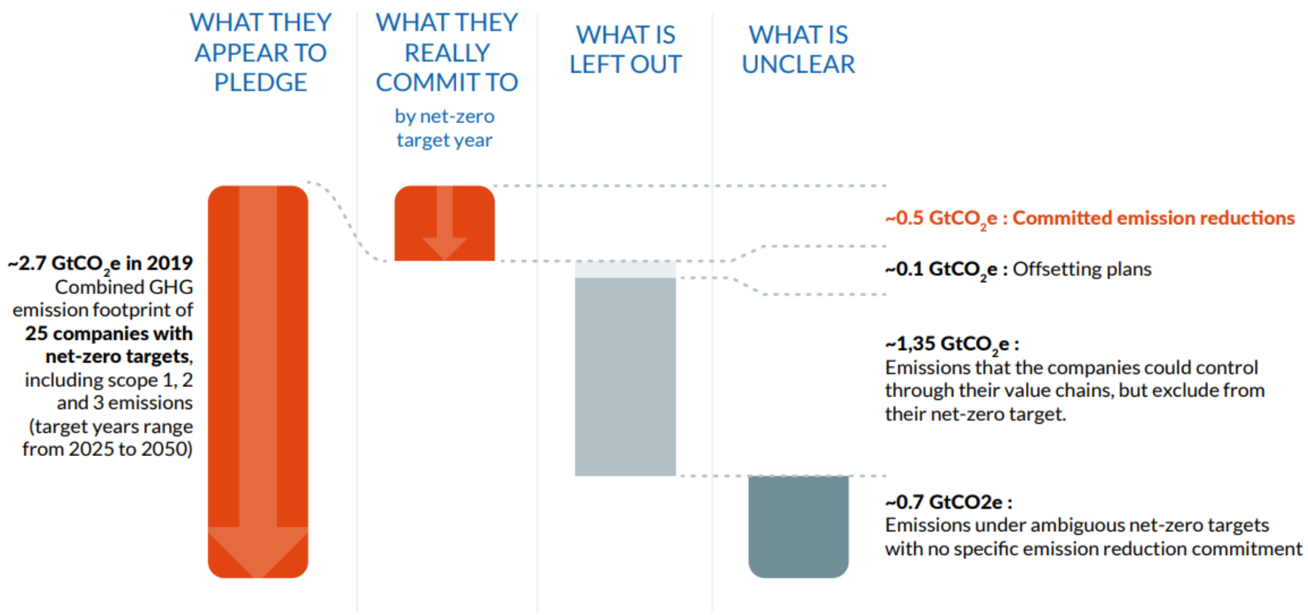
- Explain alignment with a 1.5°C pathway: As made explicit in Recital 26 CSRD, targets, emissions trajectories and plans should be compatible with meeting a 1.5°C low or no-overshoot scenario by 2050, complying with the objective of achieving climate neutrality by 2050 as established in Regulation EU 2021/1119 (European Climate Law);
- Include dates and implementing actions to achieve the near and medium-term targets: The plan should set out short (3-5 years), medium (10 years), and long-term (over 10 years) actions and interim milestones that can be used to assess progress across and within different sectors, as well as explain how these actions are in line with the 1.5°C pathway;
- Include an explanation of decarbonisation levers identified within the company's own operations and value chain, and the financial resources supporting the implementation of the transition plan;
- Be integrated into the overall business strategy and backed up by clear governance processes;
- Not rely on the use of offsets and negative emissions technologies to achieve emission reduction targets: The plan must implement absolute greenhouse gas (GHG) emission reductions in the value chain and avoid misleading neutralisation claims. Only if there are residual emissions beyond the targets which cannot be abated, these should be the subject of sinks or other offsets;
- Prioritise the closure of carbon intensive assets over their sale to third parties;
- Prioritise decarbonisation and GHG reduction, including in developing countries;[2]
- Take into account, and seek to prevent and mitigate, adverse impacts of implementing actions on workers and local communities.

[1] Compare: Draft ESRS 1: Climate change, paragraph 15. The European Financial Reporting Advisory Group (EFRAG) is appointed as the technical advisor of the Commission in the context of the development and adoption of international accounting standards in the Union.
[2] The term "developing countries" is used in reference to its meaning in Article 3 of the Paris Agreement.

b) Climate targets

There is a skyrocketing number of corporate climate pledges and a **lack of accountability and regulatory oversight.** Without specific criteria, there is a **high risk of further greenwashing** and of companies adopting plans that are merely cosmetic.[3] This risk is illustrated by the French example: Five years after the adoption of the French Duty of Vigilance Law, the first legislation having introduced corporate human rights due diligence in a legally binding framework, but which lacks specificity on climate, French companies' climate actions remain clearly insufficient.[4]

This graphical summary of the NewClimate Institute shows the lack of integrity of many net-zero commitments so far and confirms the need to specify the content and scope of this tool:[5]



Targets essentially define the ambition of a company's actions, i.e. on climate mitigation. Transition plans are the implementing arm to reach the targets and thus, **transition plans cannot be decoupled from targets** as currently proposed by the CSDDD in Article 15, paragraph 2. In alignment with the CSRD, targets should generally be required as part of the plans. This would ensure that companies that must adopt a plan do set proper targets. Otherwise, it is not clear which companies have to include targets (according to Article 15, paragraph 2: "in case climate change is or should have been identified as a principal risk for, or a principal impact of, the company's operation") and which authorities would supervise the application of such criteria.

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[3] NewClimate Institute, Net Zero Stocktake 2022.

[4] See: French Human Rights National Institution, 2021, OPINION « CLIMATE EMERGENCY AND HUMAN RIGHTS », A - 2021 - 6, p. 22 – 23.

[5] NewClimate Institute, Carbon Market Watch (Feb 2022): Corporate Climate Responsibility Monitor 2022, p. 5.

The analysis of NewClimate Institute summarises corporate practice on setting substantiated targets: [6]

SETTING SPECIFIC AND SUBSTANTIATED TARGETS	CORPORATE CLIMATE LEADERS DEMONSTRATING GOOD PRACTICE...
COVERAGE OF EMISSION SOURCES	✓ Clearly communicate the scope and year of their target. ✓ Cover all scope 1, 2 and 3 emissions (including upstream and downstream scope 3 emissions), as well as non-GHG climate forcers where relevant.
EMISSION REDUCTIONS IN THE HEADLINE PLEDGE	✓ Set a specific emission reduction target that is independent from neutralisation claims as their main headline pledge. ✓ Commit to emission reductions of at least 90% below 2019 levels, if their headline pledge is a net-zero target, to ensure that the terminology is not misleading. ✓ Set an emission reduction target that is aligned with 1.5°C compatible trajectories or benchmarks for the sector.
SUBSTANTIATION THROUGH INTERIM TARGETS	✓ Set interim targets that are aligned with the long-term vision in terms of depth and scope, with the first target on a timescale that requires immediate action and accountability (maximum 5 years). ✓ Chart a trajectory that is aligned with 1.5°C compatible trajectories or benchmarks for the sector. ✓ Prominently provide details on interim targets alongside headline pledges.

Article 15 should stipulate that all companies within the scope of application of the CSDDD have to set emission reduction targets. In alignment with the CSRD, targets should be required as an essential element of the transition plans and should be specified to:

- Include short, medium and long-term targets, including absolute GHG emission reduction targets (target values for at least the years 2030 and 2050, and milestones every 5 years in-between);
- Cover the full value chain, including scope 1, 2 and 3 emissions;
- Be based on the best available science, pursuant to the latest recommendations of the IPCC and the European Scientific Advisory Board on Climate Change, consistent with achieving 1.5°C alignment.

c) Environmental targets

A considerable inconsistency between the proposed CSDDD and the CSRD is that transition plans and **sustainability targets apply to all sustainability issues in CSRD**, not only to climate change mitigation. It would be a mistake to narrow targets and related transition plans to climate change only, especially as this file is part of the European Green Deal. Targets allow a forward-looking projection of a company's actions that is essential for addressing climate change or **biodiversity**

[6] NewClimate Institute, Carbon Market Watch (Feb 2022): Corporate Climate Responsibility Monitor 2022, p. 24.

loss and should be required for all environmental and climate impacts. Wherever relevant, targets should be based on conclusive scientific evidence and validated by an independent body with adequate scientific expertise, to ensure scientific robustness and credibility - as hinted by CSRD Article 19 (2)(b).

Article 15 should be expanded to include targets on climate change adaptation and other environmental impacts - defined in Article 3, such as biodiversity loss.

d) Remuneration

The proposal of the EU Commission to align incentives in remuneration policies remains voluntary. The provision spelled out in Article 15, paragraph 3 will have very **little effect in practice**, as it only targets companies that have already integrated sustainability matters in directors' remuneration policies.

A recent survey by Reuters of 530 corporate executives (mostly from Europe and the US) showed that only a minority of companies (20%) have partially aligned executives' remunerations with sustainability targets. Companies whose policy is to index executive remunerations with financial criteria only will not be required to change their practices.

Article 15 should link remuneration to the achievement of the targets:

- In order for the targets and transition plans explained above to have an effect on transitioning the company to a sustainable business model, it is of utmost importance to link a significant part of the variable remuneration of directors with the achievement of such targets and plans. There has to be an incentive for the directors to properly fulfil those requirements and, according to existing good market practices, linking variable remuneration has a positive effect.

e) Enforcement and board oversight

Without proper enforcement mechanisms, the lack of accountability and regulatory oversight will lead to diverging and ineffective corporate action. The French Consultative Commission on Human Rights expressed similar concerns in its 2021 Opinion on Climate Emergency and Human Rights.[7] Supervisory authorities need a clear mandate to monitor the enforcement of Article 15.

Climate obligations also need to be explicitly part of board oversight to ensure that directors are fully responsible for approving the company's strategy including targets and transition plans. Boards should have a clear obligation to ensure that sustainability risks and impacts are addressed in the company's strategy.

[7] French Human Rights National Institution, 2021, OPINION « CLIMATE EMERGENCY AND HUMAN RIGHTS », A - 2021 - 6.

Why an integral approach to climate change and environmental due diligence is key

Article 15 can strengthen and specify the obligations for corporate climate action, but it has to go hand in hand with a comprehensive approach to the definition of environmental adverse impacts in Article 3.

Article 3 should provide a definition that covers environmental adverse impacts of companies, including on climate, so that the CSDDD leaves no legal ambiguity concerning environmental and climate change due diligence, and it is clear that failures to implement the climate change obligations are subject to civil liability.

Further resources:

- For more guidance on corporate climate leadership, see WWF (2022), Beyond Net-Zero: A business pathway to spur urgent climate action towards 2030 and the Climate Science Based Target initiative.
- For a climate assessment and ranking of 27 French multinational corporate groups under the French Duty of Vigilance Law, see the "Corporate Climate Vigilance Benchmark" of the NGO Notre affaire à tous (1st edition in 2020 [here main results in English], 2nd edition in 2021, 3rd edition in 2022 [here main results in English]).
- For an overview of where climate transition plans are being mentioned in EU policies, see E3G (2022), Finance for Europe's low-carbon transition: Beyond the green label.
- For a focus on climate, environmental and land defenders, who account for nearly 70% of the attacks against defenders tracked by Business & Human Rights Resource Centre (BHRRC) in 2021, see: BHRRC (April 2022): Human rights defenders & business in 2021: Protecting the rights of people driving a just transition.
- For a ranking of the climate strategies of 25 global companies, see: NewClimate Institute, Carbon Market Watch (Feb 2022): Corporate Climate Responsibility Monitor 2022.