ClientEarth

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Factsheet - Environment and Climate

Corporate Sustainability Due Diligence Directive

The transformation to a sustainable economy is a key political priority of the European Union ("EU"), and companies have a clear role play. The recent proposal by the European Commission for a Directive on Corporate Sustainability Due Diligence ("CSDD") aims to foster sustainable and responsible corporate behaviour throughout global value chains. As a result, companies will be required to prevent and mitigate potential adverse human right and environmental impacts within their operations and value chains, as well as bring to an end and minimise actual ones. However, the proposal currently contains significant loopholes that could be used by companies to continue business as usual and disregard some of the main adverse environmental impacts that they cause or contribute to. The proposal therefore has to be substantively improved if the EU wants to deliver on its ambitions set out in the EU Green Deal.

This briefing aims at taking a closer look at climate and environmental dimension of the proposed directive and focuses on the current definition of adverse environmental impact and climate transition plan.

Does the current definition of adverse environmental impact properly capture companies' environmental footprint?

The definition of adverse environmental impact is central to halting business activities that cause and contribute to environmental harm and loss of natural resources. If the range of impacts is too narrow, the future legislation will not properly capture companies' complete environmental footprint, and ultimately fail to prevent environmental and climate damage.

The European Commission itself recognises that *"While progress has been made in recent years, the environmental impacts of consumption are still pushing us outside the safe operating space for humanity, as we exceed planetary boundaries in several ways in the EU[1]. Globally, half of all greenhouse gas emissions and 90% of biodiversity loss are caused by extracting and processing primary raw materials[2]".*[3]

All sectors from automotive, construction, chemicals, food and drink, raw material, metals, and minerals, to fashion, can be responsible for adverse environmental impacts throughout their value chains. The examples below provide an insight into some of those adverse environmental impacts.

Example 1: Food industry

Global food systems account for about a third of all greenhouse gases[4] and are responsible for major environmental impacts. These occur primarily at the production stage[5]. In the EU, agriculture, represents the greatest risk for species and their habitats, with demand for agricultural land, intensification and specialisation of practices, as well as the use of fertilisers and pesticides, constituting considerable drivers of biodiversity loss. These further contribute to polluting the air, soil, surface and ground waters[6]. Agriculture contributes to climate

change via the emission of greenhouses gases and the reduction of carbon storage in vegetation and soil.[7] Equally, fishing and aquaculture are the greatest drivers of marine ecosystem depletion, with damaging and unselective fishing gear impacting seabeds and driving unacceptable levels of bycatch, whilst aquaculture activities can be a major risk through the unsustainable use of wild caught fish for feeds. Fishing with bottom touching gear also impacts the climate as it releases as much carbon as air travel[8].

Example 2: Plastics industry

Plastics are currently used in packaging, building and construction, vehicles, textiles and electrical or electronic equipment. At all stages of its lifecycle, adverse environmental impacts can be identified (from extraction and production: use of oil and gas and greenhouse gas emissions and air pollutants; to end-of-life: litter on land and in the ocean, seas and freshwater, and greenhouse gas emissions from incineration and landfill).[9]

In the EU, there are over 50,000 plastic converting companies (mainly SMEs) with a total turnover in excess of €260 billion per year.[10] Converters transform plastic as a raw material into semi-finished and finished products for a wide array of applications, including packaging, construction and consumer electronics. One major environmental impact in the supply chain of plastics converters is plastic pellet pollution, which occurs in the production, transport and conversion of plastic. Up to 167,000 tonnes of plastic pellets are estimated to leak into the environment in Europe every year.[11] It is the largest source of primary microplastic pollution (after tyre abrasion). Good practices for handling pellets in the production, transport and conversion of plastic pellets can prevent leaks.

The examples above show the breadth of adverse environmental impacts that companies can cause or contribute to. It is therefore essential that the future legislation contains a definition of adverse environmental impact that encompasses the full range of impacts that could occur in companies' value chains, while providing companies with a good understanding of the impacts against which they will have to conduct their due diligence.

Limited approach of the European Commission to define adverse environmental impact

The European Commission has chosen a restrictive approach to define adverse environmental impact by reference to the violation of specific prohibitions and obligations of an exhaustive and limited list of environmental norms (Article 3(b) and Annex Part II of the proposal).

> Article 3(b) states: *'adverse environmental impact' means an adverse impact on the environment resulting from the violation of one of the prohibitions and obligations pursuant to the international environmental conventions listed in the Annex, Part II'*

This approach, when taken exclusively, has several limitations and might not be fit for purpose.[12] By listing only twelve specific obligations or prohibitions derived from a narrow list of environmental international agreements,[13] the Commission misses key adverse environmental impacts that can be prompted by business activities.

Firstly, not all environmental impacts that a company can cause or contribute to are (yet) covered by international conventions.[14] There is, for example, no binding international instrument on plastic pollution (negotiation for such instrument is only starting), nor for the conservation, improvement and rehabilitation of soil.

Secondly**,** the proposed list of international norms is far from complete. Some key multilateral environmental agreements are missing from the Annex Part II. The most striking example is the absence of the Paris Agreement. Other international conventions also do not appear in the Annex Part II, such as the UNECE Convention on Long-range Transboundary Air Pollution and its extended protocols or the UN Convention on the Law of the Sea.

In addition, even for the international conventions referred to in the Annex, the number of provisions listed is limited, leaving out other key provisions that could have been considered as well. That is the

case for example for the specific reference in the proposed directive to Article 10 (b) of the Convention on Biological Biodiversity, that sets out an obligation to "adopt measures relating to the *use* of biological resources to avoid or minimize adverse impacts on biological diversity". The *conservation* of biological diversity, another important objective of the Convention, is however not referred to. Yet, not all provisions and connected obligations of from international environmental conventions - which are primarly designed as agreements binding States - are formulated in a manner that can be easily translated into a practical, measurable standard of conduct for companies.

Thirdly, with the proposed approach, an adverse environmental impact would materialise only in case of a violation of a prohibition and obligation of an environmental norms. However, adverse environmental impacts can occur even in the absence of a demonstrable violation of a prohibition or obligation in accordance with such a norm. Under the Commission's current approach, companies in the fashion, chemical or food industry for example, could simply ignore their impacts on water consumption, because those impacts do not breach any pre-existing norm listed in the annex.

If we keep this approach, companies will be allowed to turn a blind eye to some of the key adverse environmental impacts in their value chain.[15]

Ultimately, the approach of the Commission is also questionable when compared to the scope of recently adopted, reviewed or negotiated EU laws. For example, in the context of the proposal for a Regulation on batteries and waste batteries, the Commission's has adopted an approach listing environmental categories. Both the European Parliament and the Council decided to be more specific and expanded the list of environmental categories that should be considered by operators when conducting their due diligence, including water and biodiversity, climate and waste.[16]

The current approach of the proposal is also at odds with the one taken in the EU Taxonomy Regulation and does not cover nor reflect in a coherent manner the six environmental objectives of that regulation: (i) climate change mitigation; (ii) climate change adaptation; (iii) the sustainable use and protection of water and marine resources; (iv) the transition to a circular economy; (v) pollution prevention and control; (vi) the protection and restoration of biodiversity and ecosystems. The Corporate Sustainability Reporting Directive has used a similar classification to identify the environmental factors that should be addressed by sustainability reporting standards.[17]

Recommendations

- Expand the definition of environmental impacts so it goes beyond references to obligations or prohibitions set out in international conventions. The definition should include a non-exhaustive list of adverse environment impacts that notably includes any adverse impact on (i) air, (ii) water, (iii) soil, (iv) biodiversity, (v) climate and (vi) the transition to a circular economy. That would ensure that the definition covers, at a minimum, the categories already covered by existing regulations and would provide a good and clear understanding of what a company will be expected to identify, assess, prevent, mitigate and account for in terms of adverse environmental impacts.
- In addition, complete the Annex with the inclusion of other international conventions provisions relevant to companies' environmental impacts, and include an option to review the Annex on a regular basis.

Is the current proposal an effective vehicle for companies' contribution to the Union's transition to a climate neutral economy?

Exclusion of climate change from due diligence obligation and weak transition plan

The absence of the Paris Agreement from the conventions listed in part II of the Annex directly undermines the Commission's reasons for and the objectives of the Proposal, i.e. "*The behaviour of companies across all sectors of the economy is key to succeed in the Union's transition to a climate-neutral and green economy in line with the European Green Deal*"[18].

The stark warnings of the IPCC reports published in 2021 and 2022 are an unambiguous reminder that the private sector must act now to mitigate their climate impacts. According to a survey done in the context of the Global Risks Report 2022, "*Climate action failure is also considered the most critical threat to the world in both the medium term (2-5 years) and long term (5-10 years), with the highest potential to severely damage societies, economies and the planet*".[19]

While the energy sector is still the largest contributor to greenhouses gas emissions (GHGs), other sectors also significantly contribute to GHGs emissions. For instance, since 1990, agriculture, which is the 2nd largest emissions sector, increased its emissions by 12%. For industrial emissions (the 4th largest sector) the increase goes up to 180%.[20]

Yet, despite the clear role that companies have to play in the transition to a climate-neutral economy, there is no obligation on these companies to conduct due diligence with respect to their climate impacts. The Commission only foresees the possibility of including adverse climate impacts as part of the due diligence requirements 7 years after the entry into force of the Directive. In circumstances where the IPCC has warned that emissions (a climate-critical adverse environmental impact), must peak no later than 2025 and must be cut by 43% by 2030 to achieve the 1.5C goal[21], the Commission's proposed timeframe would be too late.

Article 15 on "Combating climate change" that sets out an obligation for some companies to adopt a transition plan is necessary but should not give any reason to not have climate listed as an adverse environmental impact. While the establishment of a transition plan is essential and can complement and mutually support human rights and environmental due diligence obligations that bind the company, it does not negate the need for specific climate due diligence. Robust due diligence processes in companies are necessary to identify, prevent, mitigate and account for climate change impacts. Climate due diligence is also necessary to regulate the stages of operational processes which may not be subject to the obligations related to the climate plan, and to reduce the risk of adopting a plan which is merely cosmetic.

Under Article 15, it is proposed that large companies[22] shall adopt a plan to ensure that their business model and strategy are compatible with the transition to a sustainable economy and with limiting global warming to 1.5°C in line with the Paris Agreement (the climate plan). Yet, the current proposal falls short of defining the exact content of such plan. Being more prescriptive about the content of the climate plan is essential to ensure it can be an actionable instrument, and avoid it being a simple 'commitment to commit'. Otherwise, rather than procuring meaningful action by the private sector to help the EU to achieve its climate ambition, there is a predominant risk of greenwashing.

The fact that the climate plan only requires in-scope companies to identify the climate impact of the company's 'operations' is highly problematic. This means that for Scope 3 emissions – all indirect emissions that occur in the value chain upstream and downstream (GHG emissions from: (i) upstream purchasing, (ii) downstream sold products, (iii) goods transportation, (iv) travel and (v) financial

investments) – could be left at the discretion of the company whether to include them in its plan. However, Scope 3 emissions form a significant part, and commonly the majority, of many companies' climate impacts, including fossil fuel companies.[23]

Furthermore, according to the proposal, it is only when climate change has been or should have been identified as a 'principal' risk for, or a 'principal' impact of, the company's operations that the company should include 'emissions reduction objectives' in its plan. But what 'principal' means is not defined in the proposal. Moreover, companies should, in any circumstance, be required to develop and implement plans that notably (i) are evidence based and regularly updated in line with the best available science and (ii) set out short-term and medium-term absolute greenhouse gas emission reduction targets for 2025 and 2030, with a review of those targets every five years up to 2050.

It is also important to note that forward looking plans like transition plans for climate should be extended to other environmental matters like biodiversity, marine ecosystems and/or clean air.

Recommendations

- Ensure that the plan covers the company's entire value chain (scope 1, 2 and 3) and not only its own operations;
- Require companies to adopt a plan which notably (i) is evidence based and regularly updated in line with the best available science and (ii) sets out short-term and medium-term absolute greenhouse gas emission reduction targets for 2025 and 2030, with a review of those targets every five years up to 2050
- Adopt a plan on other sustainability matters like biodiversity with notably time-bound targets

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