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Law & Tax

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ESG
Key legal considerations

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Introduction

Sustainability has become an increasingly important factor in the decisions of investors, companies, consumers, shareholders and policy- and lawmakers. The broadly supported awareness for the Environmental Social and Governance ('ESG') objectives is reflected in many international voluntary standards as well as in an increasing number of European regulations towards sustainable growth.

Recent regulatory developments indicate that the ESG trend has acquired a more formal position in European and national law. Compliance with these new and often complex regulations may be challenging for companies, but offers companies the opportunity to make an appropriate contribution to a more sustainable economy. This ESG compliance poses strategic and operational challenges but will definitely create market opportunities for those who are able to adapt faster.

Furthermore, with the increased importance of ESG aspects of doing business, it is expected that more and more ESG-related litigation will be presented to courts by a large variety of parties.

For that reason, Loyens & Loeff has developed this brochure dedicated to a selection of topics so to help you navigate through this new landscape of rules.

We look forward to embarking with you on a journey to a more sustainable economy.

1. The additional Taxonomy Regulation disclosures for climate objectives

1. The additional Taxonomy Regulation disclosures for climate objectives

The first Delegated Act on sustainable activities for climate change adaptation and mitigation objectives has been published in the EU Official Journal in December 2021. This was the necessary step for the Taxonomy Regulation to (partially) enter into force. Besides a classification system, the EU Taxonomy Regulation establishes additional mandatory disclosure obligations under the Sustainable Finance Disclosure Directive ('SFRD') and the Non-Financial Reporting Directive ('NFRD').

Since 1 January 2022 Financial Markets Participants will have to make additional ('Level 1' compliant) SFDR disclosures on the taxonomy-alignment of a financial product. In addition, Large Public-Interest Entities must include in their non-financial report a disclosure on the proportion of taxonomy-eligible economic activities in relation to certain KPIs.

For SFDR or NFRD in-scope companies the additional disclosures will be mandatory but to underline their ESG efforts the disclosure can also be applied voluntary by other market participant.

1.1 The EU Taxonomy

The EU Taxonomy Regulation introduces a classification system, establishing a list of environmentally sustainable economic activities. In order to qualify as environmentally sustainable an economic activity has to meet all of the following four overarching conditions:

1. Substantially contributing to at least one of the following six environmental objectives: (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.
2. Not significantly harming any of the other environmental objectives listed under 1.
3. Complying with certain minimum social and governance safeguards such as the OECD Guidelines for Multinational Enterprises and the UN Guiding Principles on Business and Human Rights.
4. Complying with the scientifically based Technical Screening Criteria ('TSC') established by the EU Commission. These TSCs will be developed over time by Delegated Acts supplementing the Taxonomy Regulation. Firstly, the TSC for activities substantially contributing to climate mitigation and climate adaptation will be developed, followed by TSCs for the other four remaining environmental objectives listed under 1. In addition the Platform for Sustainable Finance is also preparing an advice on the expansion of the EU taxonomy to social objectives, which would also require the development of appropriate TSCs.

In December 2021 the long awaited first Climate Delegated Act has been published in the EU's Official Journal. This Climate Delegated Act covers the TSCs in relation to climate mitigation and climate adaptation for approximately 102 activities within different sectors such as among others transport, construction and real estate, manufacturing and energy.

However, natural gas and nuclear-energy activities are currently not included. In a recent advice, the Sustainable Finance Platform recommended that nuclear energy should not be considered as taxonomy aligned since the current TSC do not ensure 'do not significantly harm' (DNSH) and therefore do not meet the requirements of the Taxonomy Regulation. Despite that critical advice issued by the Sustainable Finance Platform, the EU Commission has presented its draft for the first Taxonomy Complementary Climate Delegated Act which includes amongst others TSCs for specific gas and nuclear activities that qualify as transitional activities. Once translated into all official EU languages, the Taxonomy Complementary Delegated Act will be formally transmitted to the EU Parliament and EU Council which will have six months to scrutinise the document. If not objected within this period, the draft Complementary Delegated Act is scheduled to enter into force and apply as of 1 January 2023. To ensure transparency, the taxonomy alignment of certain gas and nuclear activities would come with additional NFRD disclosure requirements (see more below).

For a practical overview of the activities currently covered and the corresponding conditions under which they could substantially contribute to either climate mitigation or climate adaptation, the EU Commission has developed the useful tool of the EU Taxonomy Compass, available online.

1.2 Additional SFDR disclosures on taxonomy-alignment

Besides establishing a classification system, the EU Taxonomy Regulation also amends the disclosure requirements in place under the Sustainable Finance Disclosure Regulation ('SFDR') and the Non-Financial Reporting Directive ('NFRD').

Since 10 March 2021 Financial Market Participants offering financial products within the EU are subject to different mandatory ESG disclosure obligations, both on entity- and on product-level. For an overview of the different disclosure obligations applicable since March 2021, read more here.

With the publications of the first Taxonomy TSCs these disclosure obligations are expanded with additional disclosure obligations which are different depending on whether the financial product aims to be dark green (article 9 products), green (article 8 products) or not at all green (article 6 products). Financial products that are market as being dark green (article 9 products) or green (article 8 products) require additional pre-contractual disclosures and periodic reporting. These disclosure obligations amongst others include information on how and to what extent the investment underlying the financial product are in taxonomy-aligned economic activities. The latter also includes the disclosure of the proportion of investments in environmentally sustainable economic activities selected for the financial products.

For green products (article 8), the Taxonomy Regulation requires the following additional statement to highlight that within the portion of investments not linked to taxonomy aligned economic activities, certain of these activities may significantly harm one of the Taxonomy Regulation's environmental objectives: 'The "do no significant harm" principle applies only to those investments underlying the financial product that take into account the EU criteria for environmentally sustainable economic activities. The investments underlying the remaining portion of this financial product do not take into account the EU criteria for environmentally sustainable economic activities.'

Products which are not promoting any ESG characteristics or not sustainable investment (article 6 products) must disclosure in the pre-contractual documentation or periodic reports the following statement: 'The investments underlying this financial product do not take into account the EU criteria for environmentally sustainable economic activities.'.

Where the Level 1 SFDR disclosures already apply since 1 March 2021, the entering into application of the SFDR Regulatory Technical Standards or 'Level 2' disclosures which include more detailed guidelines on how to report (such as templates) have been extended until 1 January 2023.

As the EU Commission aims to create a "single rulebook" which merges the SFDR and Taxonomy-related product disclosures, the European Supervisory Authorities have updated their Final Report for a single rulebook product disclosures.

Since 1 January 2022 companies must thus have to make 'Level 1' compliant Taxonomy alignment disclosure. From 1 January 2023 these disclosures will have to be 'Level 2' compliant. Where already possible, it is however recommended to align current disclosures with the future Level 2 standards (RTS SFDR) to prepare for its future entering into application as of 1 January 2023.

1.3 Additional NFRD disclosures on taxonomy-aligned and taxonomy-eligible activities

The Non-Financial Reporting Directive (NFRD) requires large public interest entities to include non-financial statements as an integral part of their annual public reporting obligations.

At present, the NFRD applies to “large public-interest entities” (‘PIEs’). Are considered being an “PIE”: (i) EU entities that have transferable securities admitted to trading on an EU regulated market; (ii) EU credit institutions; (iii) EU insurance undertakings; and (iv) EU entities that are designated by Member States as public-interest entities. “Large” here refers to a PIE with more than 500 employees and that have either a balance sheet total of more than EUR 20 million or a net turnover of more than EUR 40 million.

However it is the EU’s ambition to generally revise and extend the reporting requirements and scope of NFRD by introducing a proposal for a Corporate Sustainability reporting Directive (CSDR) (see our earlier contribution here) with the aim to expand the scope from large PIE to all large companies (listed or not).

Following the Taxonomy Regulation, the mandatory non-financial statement must include information on how and to what extent the companies’ activities are associated with economic activities that qualify as environmentally sustainable under the Taxonomy Regulation. In particular, the non-financial companies must disclose the following key performance indicators (KPIs): (i) the proportion of their turnover derived from products or services associated with taxonomy aligned economic activities; (ii) the proportion of their capital expenditure (CapEx) and (iii) the proportion of their operating expenditure (OpEx) related to assets or processes associated with taxonomy aligned economic.

In December 2021 the EU Commission’s Delegated Act and Annexes setting out the content, methodology and presentation of information to be disclosed by undertakings concerning the proportion of environmentally sustainable economic activities in their business, investments or lending activities was published in the Official Journal (‘Disclosure Delegated Act’).

From the financial year (FY) 2022, the Disclosure Delegated Act will apply for non-financial undertakings with first reporting obligations on taxonomy-alignment as from 1 January 2023. For financial institution the Disclosure Delegated Act provides an extension, as they will only have to render a first report from 1 January 2024 for FY 2023. However, as from 1 January 2022 until 31 December 2022 (or 2023 for financial institutions), undertakings must only disclose on the taxonomy eligibility of their activities.

With its proposal to also include gas and nuclear activities as transitional taxonomy aligned activities (see more above), the EU Commission also introduces additional NFRD (or future CSDR) disclosures. To provide a high degree of market transparency, financial and non-financial companies should present specific disclosure requirements to show the percentage of their gas and nuclear taxonomy aligned energy activities.

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2. The criminal angle of greenwashing?

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In a market that is becoming more conscious of the environmental (and social) impact of corporate activities, businesses in a vast array of sectors are keen to capitalise on this new trend by actively promoting their 'green' credentials. This incentive can lead to an increased risk of 'greenwashing' claims, as echoed by the recent international press. This article discusses the criminal angle of greenwashing.

2.1 What is meant by 'greenwashing'?

There is no general definition of the concept of "greenwashing" under EU law. Often, the concept is broadly described as making people believe that a company is doing more to protect the environment than it really is. However, the concept of greenwashing has received a specific definition in some recent legislative instruments. For example, in the context of the Taxonomy Regulation a specific definition is provided under Recital 11 which states that "*greenwashing refers to the practice of gaining an unfair competitive advantage by marketing a financial product as environmentally friendly, when in fact basic environmental standards have not been met*".

2.2 Have prosecuting authorities started to act upon greenwashing issues?

In May 2022, the press reported that prosecutors in Frankfurt raided the offices of an asset management subsidiary of a top-tier European bank as part of an investigation into greenwashing. The searches related to allegations of financial institutions marketing investment products as more environmentally friendly than they really were. The prosecutors were following up on accusations based on statements made by a former employee of the raided subsidiary.

There is little doubt that this kind of investigation will further develop across the EU in the next coming years. Such development may be fostered by the implementation of the whistleblowing Directive in all Member States. The "speak-up" culture that this Directive is meant to enhance might indeed lead to more reports relating to ESG-related malpractices.

2.3 How can your company best handle greenwashing allegations?

Such a scenario can on the one hand be avoided by implementing an internal early warning monitoring tool to facilitate the detection and thorough investigation of possible ESG-related misconduct. Take this as an opportunity to understand and mitigate any such problems before they become public disclosures and protect those who raise concerns or report breaches. The latter is an important part of maintaining the integrity of the company's ESG policy and is proof of the company's healthy "speak-up" culture.

On the other hand, the company should prepare for investigations into the sustainability claims that it made. In doing so, ask yourself the following questions:

1. in case of a dawn raid, who will be in charge of doing what (who will welcome and shadow investigators, who will detain ESG-related information, who will be able to answer the questions of investigators, etc) ?
2. who will be your external advisers (including for communication purposes)?
3. how will you follow-up on the raid?

2.4 What criminal charges does the company risk in Belgium?

In Belgian criminal law, no specific offence targeting greenwashing has been created so far. This does not mean, however, that the prosecuting authorities cannot fall back on other (more broadly formulated) types of offences, namely:

- Forgery (Art. 196 of the Belgian Criminal Code) : if a product is marketed as more environmentally friendly than it actually is, and if the environmental virtues of the product are misrepresented in written documents, these documents may very well be found to be forged documents. Under Belgian law, documents embedding a lie may indeed be considered as forged documents.
- Forged annual accounts (Art. 3:44 of the Code of Companies and Associations) : if the annual accounts of a company embed lies in respect of its environmental performances, these accounts may be found forged.
- Unfair practices towards consumers (Art. VI.93 and VI.97 to VI.100 of the Code of Economic Law) : misrepresentation of the environmental virtues of a product may constitute unfair practices towards consumers, which are criminally sanctioned under Book XV of the Code of Economic Law.
- Deceptive communication (Art. 33 of the Prospectus Act and Art. 25 and 40 of the Act of 2 August 2002 on the monitoring of the financial sector): under certain circumstances, the statements made by listed companies in relation to the environmental performance of their activities or investments might be found to be deceptive communication towards the market, leading to criminal sanctions.

This (unexhaustive) list of offences shows that – as most European prosecuting authorities – Belgian criminal authorities do have the means to prosecute greenwashing based on pre-existing types of offences.

2.5 Who is at risk?

Not only the company itself, but also the directors and members of the top management are at risk of prosecution for the above-mentioned offence. For the directors/top managers to be found guilty of aiding and abetting the offence, it must be established that they facilitated the offence by acting or by failing to act upon the deceptive statements, while having the knowledge and the willingness to commit the offence. In that respect, it is worth recalling that failure to act may be seen as willful blindness. For that reason, directors and top managers should make sure that they have dedicated and competent teams to whom they can delegate the monitoring of the sustainability efforts of the company they managed.

2.6 How can your company mitigate risk?

A company can mitigate these risks by avoiding wide sweeping and broad statements about sustainability efforts. For example, corporates should avoid advertisements focused solely on the end-product or service provided. Additionally, the truth is the best defence; if a company can support the statements it made with concrete sustainability efforts and firm data, they are better able to neutralize and defend the greenwashing claims. In other words, make sure that you are at all times in a position to substantiate the statements made by the company.

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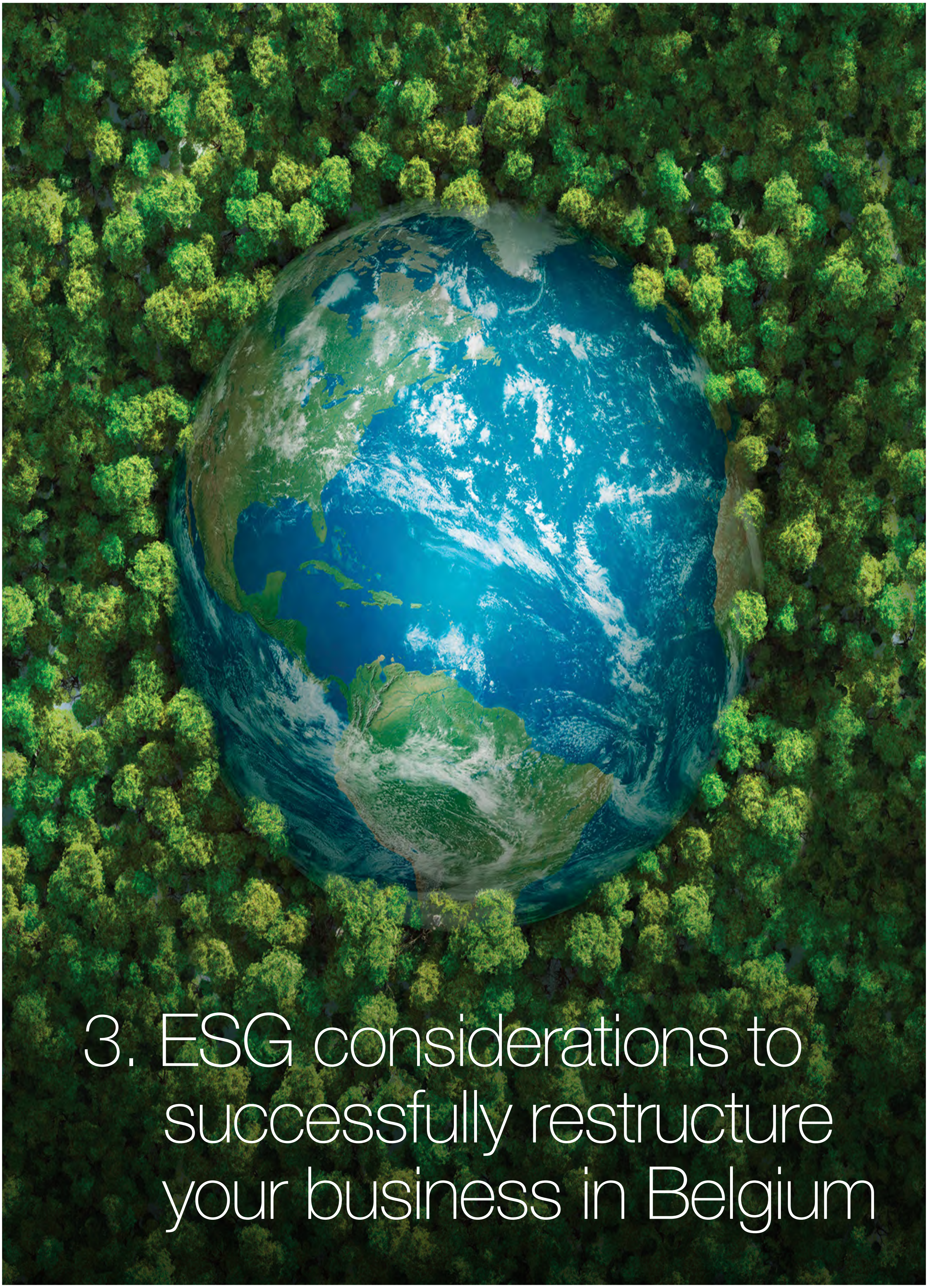

3. ESG considerations to successfully restructure your business in Belgium

3. ESG considerations to successfully restructure your business in Belgium

The current economic climate is difficult for many businesses, in particular for energy-intensive companies. The situation may deteriorate to such an extent that some companies may be faced with the choice between filing for bankruptcy or, if the business is still viable, implementing restructuring measures. IIn this article we discuss some ways in which putting Environmental, Social and Governance (ESG) issues on the top of the corporate agenda may put your business in a better position for a successful restructuring.

3.1 Introduction

Belgian companies experiencing financial difficulties have access to a whole arsenal of safeguard measures to support the continuity of their business. On the one hand, you can sit down with your main creditors and/or potential new investors to discuss on a consensual basis possible measures (*e.g.*, payment plan, new financing, *etc*.). On the other hand, your company can also apply to the court for protection against your creditors in the framework of so-called judicial reorganistaion proceedings (*gerechtelijke reorganisatie / réorganisation judicaire*). In both situations, ESG considerations are likely to come into the picture because these measures require most of the time the support of the company's existing shareholders or creditors but also the support of new investors, lenders or potential buyer(s) who exercise an increasing scrutiny on ESG factors.

3.2 Out-of-court restructuring measures

A debtor can amicably discuss restructuring measures with its creditors or with (new) investors or lenders. As financial market players themselves are increasingly the subject of stricter scrutiny (including on ESG issues), it is not uncommon to see these potential money providers imposing on the debtor ESG covenants in their loan agreements, in particular in respect of the "governance" and "environmental" part of ESG. In addition, ESG factors are becoming increasingly important for lenders and investors when assessing the overall prospects and stability of a business. Performing well on ESG criteria may therefore ease access to funding for distressed debtors. In addition, obtaining the support from all other relevant stakeholders as well (such as suppliers, employees and customers) will be equally important to successfully restructure the business. If the business' ESG values are in line with those of the stakeholders, obtaining their necessary support may prove easier.

3.3 Judicial reorganisation proceedings

The purpose of judicial reorganisation proceedings is to preserve, under court supervision, the continuity of a company in distress or its activities. It grants protection against existing creditors by allowing the company either to negotiate an amicable settlement or a collective reorganisation plan or by providing for a transfer of the company's activities to a third party.

The protection of judicial reorganisation proceedings can only be obtained if the continuity of the company is threatened in the short or medium term. In practice, the court will also examine whether the business or activities can effectively be rescued. The court may, however, only assess marginally whether there is such reasonable prospect of continuity. In other words, only if it is manifestly clear that the business or activities cannot be saved will the court dismiss the application to open judicial reorganisation proceedings.

ESG considerations may play a role in the assessment of the court and we expect that the importance of these considarations will only increase in the future. For example, if the business case of a company would be contrary to the values and objectives underling ESG criteria in such a way that it is excluded that the activities can be continued in a viable manner in the future (e.g., because the business model is not in line with the development of ESG regulation), the question can rise whether the court could (or should) not refuse the company access to the restructuring tool of judicial reorganisation proceedings.

An example that comes to mind is a car manufacturer who refuses to invest in the development of an electrical or hydrogen based car division. Making sure that your business case is viable as seen from the perspective of ESG criteria (including the EU Taxonomy Regulation's list of sustainable activities) will increase the chances your company could successfully apply for the opening of judicial reorganisation proceedings and benefit from the creditor protection that comes with is.

ESG considerations will also play a role throughout the course of judicial reorganisation proceedings. As discussed above new investors and in particular financial market players may impose strict ESG covenants as a condition to providing new financing. A potential buyer for all or part of the business is also likely to perform a due diligence with a focus on ESG compliance. In the event your company is already compliant on the ESG level (or actively working on getting there) that may facilite obtaining financing or transfering the activities to a third party.

3.4 Conclusion

Even though ESG issues are unlikely to play an all-decisive role in a business restructuring, there are nevertheless several ways in which they may impact the process or outcome. In particular, by making ESG issues a priority in your company, you may increase the likelihood of obtaining additional funding and necessary stakeholder support.

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4. Sustainability considerations in B2C relationships

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Sustainability and the environmental impact of consumer goods are becoming key drivers for consumer transactions and for advertising and marketing campaigns targeting the new generation of consumers. In this article, we discuss some ways in which Environmental, Social, and Governance (ESG) topics have made their way into consumer protection legislation (or may do so in the next couple of years). For businesses with a B2C offering, keeping a close eye on this rapidly evolving area of law is key.

4.1 What is the link between ESG and consumer protection?

In 2020, the European Parliament published the results of an analysis of the contribution of the then current EU consumer protection framework to sustainable consumption and a longer lifetime of consumer products. The study focused on various stages of the lifecycle of consumer products:

- Design and production stage (e.g., need for more ecodesign requirements and standard for durability);
- Market and pre-contractual stage (e.g., need for blacklisting of "greenwashing" claims, regulation of "green" claims for consumer products, the inclusion of mandatory pre-contractual information on durability and repairability of products and for the supply of spare parts);
- Contractual stage (e.g., need to link product warranty periods to the expected lifetime of products, more access to repair and maintenance information, making e-commerce "greener" by limiting free returns of consumer products); and
- Waste stage (e.g., measures to promote a more circular economy).

Several of these considerations and recommendations have been further developed in the past couple of years, and changes were made to consumer protection laws throughout the EU. The focus of the present article will be on Belgian law.

4.2 Promoting sustainability through enhanced product warranty requirements

The Belgian Act of 20 March 2022 (implementing EU Directives 2019/2161, 2019/770,and 2019/771) introduced some important changes in the legislative framework governing the legal warranty of conformity in B2C sales.

First, the trader's statutory product warranty no longer applies only to physical goods sold to consumers but also to the digital elements incorporated in such goods and to digital content and digital services supplied to consumers on a stand-alone basis. This legal warranty covers any lack of conformity that existed at the time of supply or delivery, and that becomes apparent within 2 years as from that moment. If the contract provides for a continuous supply of digital elements / content / services for longer than 2 years, then the liability period is the same as the supply period provided in the contract.

What's also new is that the presumption of a hidden defect already being present at the moment of delivery is now extended to the entire term of the 2-year warranty period. For physical consumer goods, this means that the burden of proof in case of a hidden defect lies with the trader (and not with the consumer) for the entire warranty period. This measure is meant to encourage traders to develop and manufacture more sustainable products. A specific warranty regime applies for the supply of digital elements / content / services.

Finally, for goods with digital elements, digital content, or digital services, B2C traders must now also ensure that consumers are informed of and supplied with all updates, including security updates, that are necessary for those goods, content, or services to keep performing "in conformity with the contract" during the entire period during which the consumer may reasonably expect this.

In case of non-conformity, the consumer shall have the right to request a repair or replacement or – in a subsidiary order – a price deduction or complete reimbursement of the purchase price. From a sustainability perspective, a clear legislative choice for repair over replacement is being recommended by stakeholders but is not (yet) reflected in the law.

4.3 Enhancing consumer awareness through pre-contractual information obligations

The Belgian Act of 8 May 2022 (also enacted within the context of implementing EU Directives 2019/2161, 2019/770, and 2019/771) introduced additional changes in the Belgian consumer law legislative framework.

Traders must now provide consumers with specific information (i) on the functionality of goods with digital elements, digital content, and digital services (including applicable technical protection measures), (ii) on any relevant compatibility and interoperability issues of which the trader is aware, or can reasonably be expected to have been aware, and (iii) of the existence of the statutory warranty period (see above).

Stakeholders are also recommending that the list of pre-contractual information obligations be updated with information on, for example, the repairability of products and sustainability warranties.

In this respect, a proposal for a new EU Directive is currently being discussed with amendments to consumer protection laws specifically aimed at empowering consumers for the green transition through better protection against unfair practices and through additional pre-contractual information to be provided by traders of consumer products. This proposal was one of the initiatives set out in the EU's New Consumer Agenda and Circular Economy Action Plan and follows up on the European Green Deal.

More precisely, the EU's proposal aims at:

- Providing information on the existence and length of a producer's commercial guarantee of durability for all types of goods, or the absence of such guarantee in case of energy-using goods;
- Providing information on the availability of free software updates for all goods with digital elements, digital content and digital services; and
- Providing information on the reparability of products, through a reparability score or other relevant repair information, where available, for all types of goods.

4.4 Greenwashing as "unfair commercial practice" in B2C relationships

The (proposed) new EU Directive mentioned above also proposes certain amendments to the list of B2C unfair commercial practices, targeting practices capable of misleading consumers away from sustainable consumption choices. Such practices include:

- Greenwashing practices (i.e., misleading environmental claims);
- Early obsolescence practices (i.e., premature failures of goods); and
- The use of unreliable and non-transparent sustainability labels and information tools.

More precisely, the EU's proposal aims at:

- Ensuring that traders do not mislead consumers about environmental and social impacts, durability and, reparability of products;
- Ensuring that a trader can make an environmental claim related to future environmental performance only when this involves clear commitments;
- Ensuring that a trader cannot advertise benefits for consumers that are considered a common practice in the relevant market;
- Ensuring that a trader can only compare products, including through a sustainability information tool if they provide information about the method of the comparison, the products and suppliers covered, and the measures to keep the information up to date;

- A ban on displaying a sustainability label that is not based on a certification scheme or not established by public authorities;
- A ban of generic environmental claims used in marketing towards consumers, where the excellent environmental performance of the product or trader cannot be demonstrated in accordance with EU Regulation 66/2010 (EU Ecolabel), officially recognised eco-labelling schemes in the Member States, or other applicable Union laws, as relevant to the claim;
- A ban on making an environmental claim about the entire product, when it actually concerns only a certain aspect of the product;
- A ban on presenting requirements imposed by law on all products within the relevant product category on the EU market as a distinctive feature of the trader's offer; and
- A ban on certain practices related to the early obsolescence of goods.

4.5 Reducing waste by putting an end to free product returns?

In the era of online shopping, an important challenge for the promotion of ESG is the generalized "right of withdrawal" that applies throughout the EU for consumer products sold online (or via other distance selling methods). In the EU, consumers have a statutory period of 14 days during which they can decide to return a product to the online trader without having to justify the return and very often without any charge. This right aims to compensate for the information asymmetry created by the fact that the consumer cannot see the goods before concluding the contract.

The current legislation provides no incentive for consumers to limit returns or to limit the environmental impact of their purchases. Legislators are therefore looking for more sustainable options. The European Parliament has also flagged this issue in its 2020 study.

In Belgium specifically, some initiatives have already been taken to make e-commerce more environmentally friendly. The Conseil Central de l'Economie has formulated several recommendations to make e-commerce, and especially the "last mile ", more sustainable. These recommendations include the use of price differentiation between sustainable (e.g., pick-up point) and less sustainable last mile delivery options and additional information to increase transparency on the environmental impact of home delivery. In practice, many online shops are implementing these recommendations by actively pointing out to consumers the environmental impact of several different delivery options, but requesting a small financial contribution to compensate for the CO2 impact of their chosen delivery option, etc.

4.6 Reducing waste by putting an end to free product returns?

As noted above, sustainability, repairability, environmental claims, etc. are currently at the heart of several proposed changes to consumer protection laws, both at European level and at national level.

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5. Belgian temporary insolvency law measures protecting energy-intensive companies

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Energy prices have soared over the last few months. Although this evolution has impacted all economic operators, energy-intensive companies are particularly affected. The Belgian legislator has therefore introduced a set of protection measures, including amongst others a so-called "temporary moratorium". This moratorium provides amongst others protection against bankruptcy and judicial dissolution as well as against attachments on movable assets for energy debts. These measures are however aimed at only protecting energy-intensive companies facing difficulties because of the increase in energy prices since the start of the war in Ukraine.

5.1 Companies eligible to benefit from the protection

The temporary moratorium only applies to energy-intensive companies in difficulty, these are companies covered by Book XX of the Code of Economic Law whose risk of discontinuity is mainly due to the increase in energy prices between 24 February 2022 and 31 December 2022. The energy sources which are taken into account are gas, electricity, coal, wood, and petroleum.

A company is only eligible to benefit from the temporary moratorium if the following cumulative conditions are met (hereafter the "Eligible Company"):

- the company was not in a situation of cessation of payments on 24 February 2022;
- the company's purchase of energy products and electricity represented at least 3% of the added value for calendar year 2021 (added value being defined as the total turnover subject to VAT, less the total purchases subject to VAT);
- in the three months before 3 November 2022, the company has paid an energy price that is at least double the average energy price paid between 1 January 2021 and 30 September 2021;
- at the moment the company invokes the protection measure(s), it does not have any outstanding and due tax or social security debts, with the exception of debts that are subject to a payment plan (excluding tax debts of EUR 1,500 or less and disputed debts); and
- the company was incorporated before 24 February 2022.

5.2 Protection measures

The temporary moratorium consists of the following protection measures.

5.2.1 Protection against attachments on movable assets

If an attachment is laid on movable assets for debts incurred after 24 February 2022 for the purchase of energy products, the Eligible Company can request the court to lift the attachment provided it demonstrates all conditions set out above are met. Attachments on immovable assets (*onroerend beslag / saisie immobilière*), however, remain possible.

The temporary moratorium does not release Eligible Companies from the payment of their debts for the purchase of energy products as they fall due. Interests will therefore continue to accrue on those debts, however at the statutory interest rate (currently 1.5%), unless the contractually agreed interest rate is lower. In addition, a contractual damages clause (*schadebeding / clause pénale*) will be without effect for the non-payment or the late payment of energy debts.

5.2.2 Protection against bankruptcy and judicial dissolution

An Eligible Company cannot be declared bankrupt or be judicially dissolved, unless at the request of the public prosecutor or a provisional administrator appointed by the court, following a referral of the chamber for enterprises in difficulties, or with the consent of the company itself. In addition, an Eligible Company who is in a state of bankruptcy cannot be summoned in forced transfer of its activities in the framework of judicial reorganisation proceedings (*gerechtelijke reorganistie door overdracht onder gerechtelijk gezag / reorganisation judiciaire par transfert d'entreprise sous autorité judicaire*).

A company summoned in bankruptcy or dissolution at the initiative of a person other than the public prosecutor or a provisional administrator (in practice this will mainly mean by a creditor), will have a period of minimum 15 days from the preliminary court hearing (with possible court's extension) to provide evidence that it is an Eligible Company that must benefit from the temporary moratorium. If the debtor does not appear at the court's hearing, it will be presumed not to be an energy-intensive undertaking in difficulty.

Also, the statutory obligation for an Eligible Company to file for bankruptcy is suspended provided the conditions for bankruptcy are met due to the increase in energy prices. The suspension of the obligation to file for bankruptcy also implies that the criminal sanctions applicable to directors for late filings are not applicable.

5.3 Entry into force

The temporary moratorium entered into force on 3 November 2022 and will apply until 31 March 2023 with possible adjustment and extensions.

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6. Trends in climate litigation

6. Trends in climate litigation

A global spike in court cases over climate change demonstrates the increasing role of litigation in addressing the climate crisis. Governments, banks and large corporations around the world are confronted with a rapid increase in climate litigation cases and Belgium is not being left behind. Climate litigation is being used as a tool to advance climate action or to challenge the way in which climate policy is being implemented. In recent years, a specific increase can be noticed in climate cases involving corporate defendants in the energy (oil, gas and coal) sector as well as in other sectors.

6.1 What is meant by 'climate litigation'?

According to the United Nations Environment Program (UNEP), climate litigation refers to cases brought before administrative, judicial and other investigatory bodies that raise issues of law or fact regarding the science of climate change and climate change mitigation and adaptation efforts.

For more information, see UN environment programme (unep.org).

6.2 What are the current global trends in climate litigation?

In June 2022, the London School of Economics (LSE) published a report on global trends in climate litigation. This report looks at developments in climate litigation from May 2021 to May 2022 and identifies the areas where climate litigation cases are likely to increase in the future.

The number of climate litigation cases in the world has more than doubled since 2015. The total number of cases was over 2,000 in May 2022, with approximately one fourth of them being filed between 2020 and 2022. Outside the United States, Australia, the UK and the EU remain the jurisdictions with the highest volume of cases.

Climate litigation cases are often being used to enforce or enhance climate commitments made by governments. Recently, there has also been a noticeable increase in climate cases against fossil fuel companies as well as corporate actors active in the plastics, food and agriculture, finance and transport sectors. Another noticeable increase is the number of climate litigation cases with the strategic ambition to increase action from countries and scale back the use of fossil fuels in the energy sector.

According to the LSE report on global trends in climate litigation, there are five areas to watch:

- Cases involving personal responsibility;
- Cases challenging commitments that over-rely on greenhouse gas removals or negative emissions technologies;
- Cases focused on short-lived climate pollutants;
- Cases explicitly concerned with the climate and biodiversity nexus; and
- Strategies exploring legal recourse for the loss and damage resulting from climate change.

For more information, read Global trends in climate change litigation: 2022 snapshot.

6.3 What kind of climate cases have been initiated in Belgium so far?

According to climatecasechart.com, a U.S. website providing a global database of climate change case law per jurisdiction, and climate-laws.org, a website of the Grantham Research Institute at LSE and the Sabin Center at Columbia Law School also providing a global database of climate litigation cases per jurisdiction, five climate cases can be found in Belgium:

6.3.1 VZW Klimaatzaak v. Kingdom of Belgium & Others

This case concerns the question whether federal and regional governments can be compelled to reduce greenhouse gas emissions.

The case was brought by an organization of concerned citizens (Klimaatzaak) and 58,000 citizen co-plaintiffs, arguing that Belgian law requires the Belgian government's approach to reducing greenhouse gas emissions to be more aggressive. The case was initiated against the Belgian State, the Walloon Region, the Flemish Region, and the Brussels-Capital Region as defendants.

The plaintiffs called for greenhouse gas reductions of 40% below 1990 levels by 2020 and 87.5% below 1990 levels by 2050. The plaintiffs requested a court injunction directing the Belgian governments to reduce emissions 42 to 48% in 2025 and at least 55 to 65% in 2030.

On 17 June 2021, the Brussels court of first instance decided that the federal state and the three regions jointly and individually breached their duty of care by failing to take necessary measures to prevent the harmful effects of climate change, but declined to set specific emission reduction targets on separation of powers grounds.

On 17 November 2021, Klimaatzaak appealed the decision of the Brussels court of first instance refusing to set specific binding targets related to the reduction of greenhouse gas emissions over time.

For more information, see VZW Klimaatzaak v. Kingdom of Belgium & Others - Climate Change Litigation (climatecasechart.com) or VZW Klimaatzaak v. Kingdom of Belgium, et al. (Court of First Instance, Brussels, 2015) - Belgium - Climate Change Laws of the World (climate-laws.org)

6.3.2 ClientEarth v. Belgian National Bank

This case concerned the question whether the Belgian National Bank's purchasing of bonds from fossil fuel companies violated EU law.

On 13 April 2021, ClientEarth initiated court proceedings against the Belgian National Bank claiming that the latter would fail to meet environmental, climate, and human rights requirements when purchasing bonds from fossil fuel and other greenhouse-gas intensive companies. In December 2021, the Brussels court of first instance dismissed ClientEarth's claim on procedural grounds. Early 2022, ClientEarth appealed this decision but later withdrew its claim.

For more information, see ClientEarth v. Belgian National Bank (climatecasechart.com) or ClientEarth v. Belgian National Bank (climate-laws.org).

6.3.3 Carbon Market Watch v. FIFA

This case concerned the question whether FIFA's advertising of the 2022 World Cup in Qatar as "carbon neutral" was misleading and false.

In December 2022, Carbon Market Watch, a not-for-profit association, filed a complaint against the Fédération Internationale de Football Association (FIFA) with the Belgian advertisement ethics panel. Similar claims were simultaneously filed in France, the Netherlands, the United Kingdom, and Switzerland. Carbon Market Watch alleged that FIFA's advertising of the 2022 World Cup in Qatar as "carbon neutral" was misleading and false. The relevant authorities in Belgium, France, the Netherlands, the United Kingdom, and Switzerland announced that all five complaints would be examined jointly by the Swiss authorities.

For more information, see Carbon Market Watch v. FIFA (climatecasechart.com) or Carbon Market Watch v. FIFA (climate-laws.org).

6.3.4 Lauwrys A.O. v. The Province of Antwerp

This case concerned the question whether a new gas station project in Boechout complied with the climate objectives under the Flemish Code for Spatial Planning.

On 3 April 2019, a company requested an environmental permit to build and exploit a new gas station in Boechout, a municipality located in the Flemish province of Antwerp. The municipal authority refused to deliver the permit because the envisaged gas station was not "future proof". It did not include a recharge point for electric cars nor did it provide for compressed natural gas.

The requesting company appealed this decision, but the local authorities again rendered a negative decision. However, the provincial government eventually decided, on appeal, that the project should receive an environmental permit on the ground that the reason used by the local authorities to refuse to deliver the permit was illegal.

After the permit had been delivered, prospective neighbors of the envisioned gas station sought to suspend and annul the environmental permit before the Council for Permit Disputes. The Council decided that the environmental permit was not carefully motivated because there was no research on whether the project would be compatible with the environmental objectives of the community of Boechout or whether mitigating measures would be sufficient to compensate the negative advice of the community of Boechout. On this ground, the Council suspended the decision of the provincial government on 22 April 2021.

In the proceedings on the merits, which sought to annul the permit, the Council found on 9 December 2021 that there was insufficient justification with regard to the gas station's compatibility with the residential area in which it was to be built and with its immediate surroundings and, as such, annulled the environmental permit.

For more information, see Lauwrys A.O. v. The Province of Antwerp (climatecasechart.com) or Lauwrys A.O. v. The Province of Antwerp (climate-laws.org).

6.3.5 ClientEarth v. Flemish Region

This case concerns the question whether the approval by the Flemish authorities of INEOS' Project One is illegal under EU and Belgian laws due to INEOS' inadequate assessment of how the project would impact the climate.

In 2021, Flemish authorities announced their approval of petrochemicals giant INEOS' plastics plant project ('Project One') in the Port of Antwerp.

ClientEarth and 13 other NGOs argue that this project would have tremendous and inadequately assessed environmental impacts, namely in the form of plastic pollution and climate change exacerbation. As a consequence of these concerns, these NGOs appealed the permit with the Environmental Ministry of Flanders in early 2022. The appeal was dismissed in June 2022.

A month later, the NGOs announced that they would bring the Flemish authorities to court to challenge the decision to dismiss their appeal. They argue that INEOS failed to present an adequate assessment of how the project would impact the climate, nature and surrounding air quality and that the Flemish authorities approved the project without first fully assessing its impacts, making the approval illegal according to EU and national laws. These proceedings are currently pending before the Council of Permit Disputes.

For more information, see ClientEarth v. Flemish Region (climatecasechart.com) or ClientEarth v. Flemish Region (climate-laws.org).

This list of Belgian climate litigation cases is not exhaustive.

Another known climate litigation case in Belgium is "De Luchtzaak". In 2017, Greenpeace initiated court proceedings before the Brussels court of first instance against the Flemish government for doing too little against air pollution, and specifically against the exceedance of European standards for nitrogen dioxide (NO2). The Brussels court of first instance, the Brussels attachment judge and the Brussels court of appeal all ruled in favor of Greenpeace.

6.4 How will climate litigation in Belgium evolve?

The above overview demonstrates that climate litigation is clearly on the rise in Belgium. However, this is nothing yet compared to the spike in climate cases that can be seen in other jurisdictions, such as the United States, Australia, the UK and the Netherlands. Whereas in Belgium most climate litigation cases have been directed against the government so far, other jurisdictions demonstrate that climate litigation is on the rise against corporations in different industries too.

In the Netherlands, for example, climate litigation cases have been brought against large corporations, such as Shell (as large producer of fossil fuels), KLM (as large consumer of fossil fuels) and Pension Fund ABP (as major financier of / investor in the fossil industry).

In the landmark case Milieudefensie et al. v. Royal Dutch Shell plc., the court of The Hague ordered Shell on 26 May 2021 to reduce its emissions with 45% by 2030, relative to 2019, across all activities, including both its own emissions and end-use emissions, on the basis of the unwritten standard of care. The court held that there is broad international consensus (soft law) that every company should independently work towards the Paris target of net zero emissions by 2050. The court held that because of the weighty interests (fundamental rights) served by the reduction obligation, Shell must do its part in respect of the emissions over which it has control and influence over, and that this is an independent responsibility of Shell, from whom - because of Shell's specific circumstances - much can be expected.

It is likely that this trend of climate litigation cases against corporations will also continue in Belgium. Belgian banks, institutional investors and other large corporations should be aware of this risk.

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7. Enforcing ESG obligations in supply contracts

7. Enforcing ESG obligations in supply contracts

Now that companies are facing increasing scrutiny of their ESG practices by regulators, investors, customers, and the public at large, supply chain management and related ESG commitments (including the audit and enforcement hereof) are also receiving increased attention. Whether in the context of legal obligations to conduct ESG due diligence throughout the company's supply chain, or simply to implement the company's voluntary sustainability standards, ESG clauses should be appropriately drafted to ensure that they lead to the desired result.

7.1 Origin of ESG clauses

ESG clauses are a contractual instrument used by companies to encourage, demand or oblige their suppliers to improve their ecological and/or social governance and to take sustainable, climate-friendly and ethically aligned actions. Additionally, they are a way to address investors' and customers' (including consumers', see here) concerns in this field and to address such concerns in every step of a supply chain.

Incorporating ESG standards into contracts throughout the supply chain can have several commercial benefits, such as improving customer relationships and reputational benefits for companies being seen as ecological and socially conscious. Additionally, ESG ratings and legislative initiatives requiring disclosure and reporting of environmental and social risks are rising. In this context, organizations such as the Organization for Economic Co-operation and Development (OECD) and the United Nations (UN) have recommended that companies influence their suppliers through contractual agreements to maintain and improve sustainability and responsible business conduct.

Additionally, in the EU, the proposal for a directive on corporate sustainability due diligence , which aims to foster sustainable and responsible corporate behaviour throughout global value chains, will soon require companies to seek contractual assurance from their business partners to ensure compliance with their sustainability goals and to perform ESG due diligence throughout their supply chain.

In this context, ESG clauses are increasingly inserted into commercial contracts. However, the way in which such clauses are drafted has a significant impact on how they are interpreted and enforced.

7.2 Different types of ESG clauses

ESG clauses come in different shapes and sizes and can relate to, inter alia, (i) environmental decisions, such as the use of specific products or packaging, shipment requirements, etc; (ii) human rights and the prohibition of engaging in child labor or the obligation to provide a healthy and safe work environment; and (iii) obligations to withhold from engaging in or working with companies linked to corruption, drugs of arms trafficking.

The way in which ESG clauses are drafted will significantly impact their scope, interpretation and enforceability. Below, we will highlight five key considerations for any contractual ESG commitment.

7.3 Key contractual considerations

As a preliminary note, whenever a supplier is asked to respect (internal or external) codes of conduct, policies or guidelines, such documents should be duly communicated to and known by the supplier, who needs to accept to be bound by them. Ideally, this is done by including these documents in the contract itself (for example, as an annex) or by providing a copy of the relevant documents to the supplier prior to the conclusion of the agreement and having the supplier sign for acceptance hereof. A mere reference to the existence of such documents (e.g., in general terms and conditions) or a link to the company's website may lead to enforceability issues. The supplier could argue that it was not made aware of the required commitments and their extent. This will be especially true in case of internal policies or guidelines that are not widely known or which the supplier cannot be (reasonably) expected to know. The same consideration applies to any unilateral amendments made by the company to its codes of conduct, policies or guidelines.

7.3.1 Nature of the ESG commitment

In the light of the specific activities performed by a contracting party, it is important to evaluate the environmental and social risks its suppliers are exposed to and the extent to which they may pose risk to the company, its investors and its customers.

Once these risks or concerns have been identified, it is important to define them clearly and measurably in an enforceable contractual commitment. Any ESG clause must be drafted so that it is straightforward, for both contracting parties, (i) what is expected from the supplier, and (ii) how such expectation must be met. For example, if an ESG clause provides that the supplier must "act in an environmentally conscious manner" or "perform its activities ethically", interpretation disputes may arise and it will be difficult to conclude at what point (and to which extent) the supplier will have (materially) breached this undertaking. Adding more specific targets and milestones reduces this risk.

Second, companies will need to decide whether the ESG commitments of their suppliers should be an obligation of means (i.e., a "best efforts" obligation) or an obligation of result within the meaning of Article 5.72 of the new Civil Code. For example, is it sufficient that the supplier uses all reasonable efforts to reach an expectation, or does it need to achieve a specific, measurable result?

The answer to this question will play an essential role when deciding whether the ESG commitment was met (or breached). More specifically, a party bound by an obligation of means commits itself (only) to use all reasonable efforts an ordinary, prudent contracting party of the same specialty would use in like circumstances. In other words, if the supplier fails to reach the expected commitment, it will not automatically be in breach of the contract. It will be for the company to prove the fault of the supplier. For this type of clauses, it may be helpful to include specific (measurable) indicators to assess the supplier's efforts (e.g., by demonstrating what efforts should as a minimum be made). Conversely, if a party is bound by an obligation of result, the contractual fault is presumed from the moment the outcome has not been achieved and it will be for the supplier to prove that it was not at fault (i.e., that the result was not achieved due to force majeure). The clause itself must include all relevant indicators to assess the supplier's behaviour.

7.3.2 "Essential" nature of the ESG commitment

Contractual clauses that are deemed "essential" for a contract to exist offer additional legal protection in various manners. For example, by explicitly designating an ESG commitment as an essential clause in a supply contract, a breach of this clause may more easily be invoked as a reason to unilaterally terminate the contract. Additionally, the supplier will in principle not be able to invoke a contractual exoneration clause to escape the performance of its essential obligations under an agreement. Conversely, the inclusion of ESG clauses in the company's general terms and conditions, beyond the above-mentioned enforceability issues that it raises, leads to the presumption that they do not constitute an essential or substantial element of the contract, but only an accessory element.

7.3.3 Enforcement of the ESG commitment

Linking a specific consequence to the breach of an ESG clause will not only encourage suppliers to actually comply with their contractual ESG commitments, but will also provide the company with a clear solution in the event such obligation is not met.

Traditionally, parties could opt for (i) damages or (ii) a suspension or termination right (or a combination of both).

For ESG clauses specifically, it can be challenging to assess and quantify the damage suffered as a consequence of the breach (e.g., reputational damage). To mitigate this risk, parties could include a lump-sum indemnity which will be automatically due in case of a breach of the ESG clause. Important to keep in mind, however, is that the indemnity should still be meant to cover only the (potential) foreseeable damages in case of a breach of the ESG clause, but cannot be 'punitive' in nature. Alternatives are to require the breaching supplier to perform a certain obligation in kind or to donate to a recognized human rights or climate organization.

Finally, when opting for a unilateral suspension or termination right, parties should ideally indicate in their agreement that a violation of the ESG clause will be considered sufficiently serious to justify such action. In the absence thereof, the seriousness of the breach and its consequences for the contractual relationship will have to be assessed by a court, on the basis of all relevant circumstances.

7.3.4 ESG documentation & audits

The enforceability of ESG clauses very much depends on the company's ability to verify and monitor the supplier's compliance with the obligations imposed by these clauses. Contracts therefore often include obligations for the supplier to proactively report on any progress made with respect to its ESG commitments, to regularly provide updated compliance documentation or certificates, to have an internal/external audit process, etc.

Additionally, ESG clauses are typically enforced through audit rights. ESG 'due diligence' in a supply chain context can include the involvement of technical, social, environmental and other experts. Several auditing and consultancy firms already provide tailor-made services for companies to carry out ESG due diligence in their supply chain. Typically, this type of audit does not only cover the company's direct supplier, but also its own agents and subcontractors 'down the chain'.

Finally, note that reporting and audit clauses can be tailored to the needs of the contractual relationship by including specific modalities. For example: audits to be conducted only during business days and during specific hours, audits only upon (reasonable) prior notice (or, conversely, without notice), possible involvement of a third-party auditor (which needs to have an international expert recognition), interval between audits, cost of the audit, confidentiality safeguards, etc.

7.3.5 Duplication of the ESG commitment throughout the supply chain

ESG clauses often provide for the obligation for the supplier to “pass-through” or duplicate its own ESG commitments (or essentially equivalent commitments) in relation to its own suppliers or subcontractors. Also this obligation can be included in the form of an obligation of means (“best efforts) or in the form of an obligation of result.

Additionally, the ESG clause could provide that the supplier’s own suppliers or subcontractors need to countersign the company’s code of conduct or ESG policy and that the supplier should provide a copy hereof to the company. As the chain is of course only as strong as its weakest link, the contract could also state that the company should provide its express written approval before any subcontractor can be engaged, and such subject to prior ESG due diligence. Again, this type of clause can take many forms.

7.4 What’s next?

ESG commitments have become an important part of many supplier contracts and supply chain risk management. However, to have the desired effect, one must pay attention to how these clauses are drafted and to which consequences such clauses may lead. Companies are advised to review their contract templates and (where needed) to update their supply contracts to ensure that they can successfully request their suppliers to take actions or decisions that are aligned with their environmental, social, and ethical goals, and to verify compliance with such commitments through supply chain due diligence.

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8. Proposal for a corporate sustainability due diligence directive

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On 23 February 2022, the European Commission published its proposal for a Corporate Sustainability Due Diligence Directive (hereinafter called CSDD Proposal) requiring companies to implement certain processes throughout their value chains in line with ESG-criteria. The CSDD Proposal ties into the broader framework of EU ESG related legislative initiatives and provides a substantive backbone for the reporting obligations thereunder.

8.1 Personal scope of application

While the initial proposal from the European Parliament included a broader scope (also capturing listed SMEs and SMEs active in high-risk sectors), the scope of the CSDD Proposal is limited to (very) large companies divided into two groups.

The first group consists of EU companies that had more than 500 employees on average and had a net worldwide turnover of more than EUR 150 million in the last financial year for which annual financial statements have been prepared.

The second group consists of EU companies active in certain so-called high risk sectors that do not reach the above thresholds but had more than 250 employees on average and had a net worldwide turnover of more than EUR 40 million in the last financial year for which annual financial statements have been prepared, provided that at least 50% of the net turnover was generated in one or more high risk sectors, including manufacturing, wholesale and trade of textiles, clothing and footwear, agriculture, forestry, fishery, and the extraction of mineral resources. In addition, the CSDD Proposal, in its current form, will apply to non-EU companies as well if they fulfill either of the net turnover criteria mentioned above for EU companies.

It is estimated that based on the above criteria, ca. 17,000 companies active in the EU would fall directly within the personal scope of application of the CSDD Proposal.

8.2 Due diligence obligations

The companies in scope of the CSDD Proposal will be required to conduct human rights and environmental due diligence by carrying out the following actions, in line with prior OECD Guidance for Responsible Business Conduct:

1. integrating due diligence into their policies (Article 5);
2. identifying actual or potential adverse impacts (Article 6);
3. preventing and mitigating potential adverse impacts, and bringing actual adverse impacts to an end and minimising their extent (Articles 7 and 8);
4. establishing and maintaining a complaints procedure (Article 9);
5. monitoring the effectiveness of their due diligence policy and measures (Article 10);
6. publicly communicating on due diligence (Article 11).

The due diligence obligations do not just pertain to the company itself, but also to its subsidiaries and their operations, as well as operations carried out in the value chain by established business relationships.

To properly understand the scope of the due diligence obligations, a number of key concepts have been defined in the CSDD Proposal:

- **adverse impact** is defined in relation to violation of prohibitions and obligations set out in international environmental or human rights conventions listed in an Annex to the CSDD Proposal;
- **established business relationship** is defined as a direct or indirect business relationship which is, or which is expected to be lasting, in view of its intensity or duration and which does not represent a negligible or merely ancillary part of the value chain;
- **value chain** is defined as activities related to the production of goods or the provision of services by a company, including the development of the product or the service and the use and disposal of the product as well as the related activities of upstream and downstream established business relationships of the company (with specific derogations for Regulated Financial Undertakings).

In addition to the general due diligence obligations, Group 1 companies, whether formed in accordance with the laws of the EU or not, need to establish a plan ensuring that their business strategy is compatible with limiting global warming to 1.5° C in accordance with the Paris Agreement. If climate change is identified as a principal risk for, or principal impact of, a company's operations, the company must also include emission reductions objectives in its plan.

8.3 Directors' duties

The CSDD Proposal also has a corporate governance impact by imposing a specific duty of care on directors. Article 25 of the CSDD Proposal provides that when fulfilling their duty to act in the best interest of the company, directors of companies take into account the consequences of their decisions for sustainability matters, including, where applicable, human rights, climate change and environmental consequences, including in the short, medium and long term. Additionally, Member States must ensure that their laws, regulations and administrative provisions providing for a breach of directors' duties apply also to the provisions of Article 25.

8.4 Enforcement

The CSDD Proposal includes a combination of administrative enforcement and civil liability to monitor and ensure overall compliance with the obligations set forth therein.

Member States must designate one or more national authorities for supervision. For third country companies, the competent authority will be that of the EU Member State where they realise the biggest part of their turnover. The EU Commission will set up a European network of national supervisors for a coordinated approach, similar to other areas of EU law (e.g. ESMA in respect of securities and financial markets).

According to the CSDD Proposal, national authorities should have the power, among other things, to request information, to carry out investigations and to impose administrative orders and sanctions in the event of non-compliance. Such administrative sanctions should be effective, proportionate and dissuasive.

In addition to the administrative sanction mechanism, the CSDD Proposal requires Member States to establish a civil liability regime for companies for damage suffered by victims due to a company's failure to exercise due diligence and take appropriate measures to end identified adverse impacts. EU Member States must ensure that the civil regime for the liability of companies has an overriding mandatory application, so that civil liability cannot be denied on the sole ground that the law applicable to such claims is not the law of a Member State.

It should be noted that, assuming compliance with Articles 7 and 8 of the CSDD Proposal, a company shall not be liable for damages caused by an adverse impact arising as a result of the activities of an indirect established business relationship, unless it was unreasonable for the company to expect, in the specific circumstances of the case, that the actions taken in accordance with Articles 7 and 8 would be adequate to prevent, mitigate, bring to an end or minimise the extent of the adverse impact.

8.5 Legislative process

Since the publication of the CSDD Proposal, the EU legislative process has been ongoing with the European Parliament and the Council of the European Union reviewing the CSDD Proposal.

On 1 December of last year, the Council has adopted its agreed negotiating position on the CSDD Proposal. This agreed negotiating position included a number of key amendments to the CSDD Proposal, including:

- reduced personal scope of application: the turnover and employment criteria would need to be met for two consecutive financial years rather than only in the last financial year;
- the concept of “established business relationship” is abandoned and replaced by “business partner”;
- the risk-based approach was strengthened by amending Article 6 (mapping and in-depth assessment of adverse impacts) and introducing a new Article 6a on prioritisation of adverse impacts;
- “value chain” is replaced by “chain of activities” reflecting a shift to a supply chain focus rather than the entire value chain;
- the decision of whether or not to include the provision of financial services by regulated financial undertakings is left up to each Member State;
- in respect of the requirement to combat climate change, the text of the CSDD Proposal has been amended to more closely align with the Corporate Sustainability Reporting Directive;
- the civil liability provisions were significantly amended, including clarifications on the conditions for civil liability (including fault) and the right to full compensation for victims was enshrined but provisions were also included to avoid overcompensation;
- Article 25 and 26 of the CSDD Proposal on the duties of directors were deleted;
- finally, a more gradual phase-in approach was adopted regarding the application of the rules in the CSDD Proposal, whereby the CSDD Proposal’s provisions would become applicable to a new category of the largest companies (>1,000 employees and >EUR 300 million worldwide net turnover) three years following entry into force of the CSDD Directive, four years for Group 1 companies and five years for Group 2 companies.

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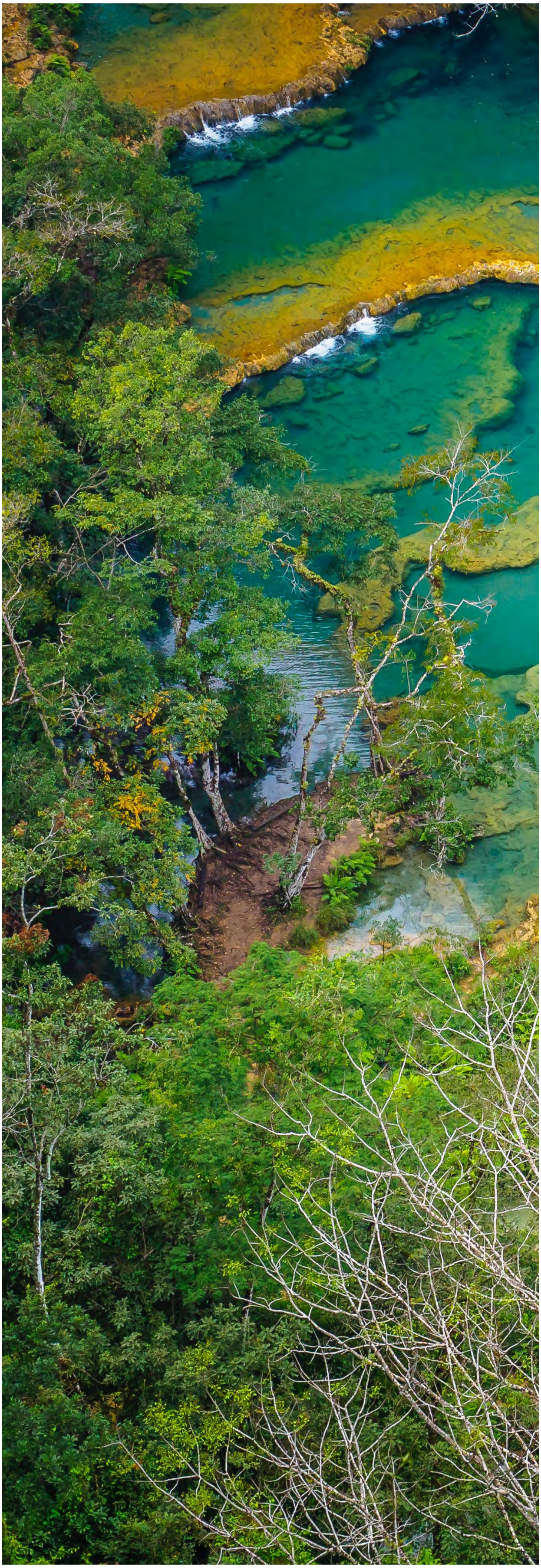

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