Climate Pledges, What Now?

Brief Reflections on the Impact of Corporate Climate Pledges

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Introduction

Climate pledges are an ever growing means for committing to reach net zero carbon emissions by 2030-2040. Although climate pledges could be celebrated by society and other environmental stakeholders, these pledges may carry long term consequences to their corporate pledgors if not properly reasoned or implemented. This blog briefly discusses some of their potential impacts.

National Climate Pledges

On 12 December 2015, 196 parties signed the Paris Agreement, an international legally binding treaty on climate change to limit global warming. It entered into force on 4 November 2016, binding its signatories to an agreed common framework under which critical national climate action is pledged and communicated to the United Nations Framework Convention on Climate Change as 'nationally determined contributions' (or 'NDCs').

The United Kingdom's inaugural NDC in 2015 aimed at a 53% cut in carbon emissions, a target aligned with the European Union, despite having set out a domestic target of 57%. Both targets did not reflect the United Kingdom's full potential, which was closer to 69%. The Climate Change Act 2008, s. 1(1) ordained an ultimate target of a 'net UK carbon account for the year 2050' of at least 100% lower than the 1990 baseline. In late 2020, the United Kingdom communicated a new NDC committing to a 68% reduction by 2030, compared to 1990 levels.

Considering these developments, climate action has shifted from state-level and NGO-led activism, to vociferous corporate shareholders using their power to impel corporate directors to take climate action. Thus, how has the outlook of corporate climate pledging adapted to this transnational impetus?

Corporate Climate Pledges

Beneath the national climate action framework lies corporate climate action across the economy. Corporations have taken their own initiatives to combat climate change, setting voluntary goals, targets, and pledges. Yet, there seems to be very few – if any – viable mechanisms in place to hold these corporations accountable for their pledges.

Resultingly, there has been a precipitous rate of environmental stakeholders turning to legal process to enforce these pledges against their pledgors. For example in the Dutch case of *Milieudefensie et al. v. Royal Dutch Shell plc*, the Hague District Court found that the directors of Royal Dutch Shell owed a standard of care under the Dutch Civil Code to reduce global emissions of their company by 45% by 2030 (compared to 2010 levels). The lawsuit is one of many in a growing stream of climate litigation, as contained in the Gratham database as of late 2022.

Three impediments to how these pledges are realised were found in writing this article. The first issue concerns the lack of standardisation of how extant emissions are quantitatively measured by corporations retrospectively across different sectors (Peel 2011). One way to achieve this is to cultivate formulas designated for the specific nature of the socioeconomic activity carried out by the corporation. A constructive measure would be to also establish what the Irish Government has dubbed 'sectoral emissions ceilings', from which corporations can gauge their targets and derive appropriate formulations based on the sector(s) they fall under.

The second issue concerns credibility and the lack of trust towards pledgors presenting perfidious assertions regarding their environmental performance. This cleft in credibility has intensified the spotlight on transparency and accountability for greenwashing (or climate disinformation). The response to greenwashing has been stringent, sometimes even severe, as in the case of Deutsche Gesellschaft für Wertpapiersparen (or 'DWS') where the police raided its offices after allegations of having misled investors about their environmental performance and products. The overarching response to greenwashing has been to promote the regulation of environmental marketing, and benchmarking corporate net zero targets, akin to the Net Zero Tracker. The reaps of these fruits are yet to materialise.

Save where climate pledges are legitimised, a third issue arises concerning the legal enforceability of these pledges. For example, in England and Wales, the law of contract is plausibly the first concerned in enforcing climate pledges, and potentially, tort, should forthcoming climate litigation succeed in establishing a duty of care between corporate directors and shareholders. However, for now, the scope for establishing a tortious liability (i.e., a duty of care) remains uncertain, if not unlikely, despite proposals to introduce a 'corporate duty of environmental care' to company law.

Financial Dichotomy

Many corporations fail at contextualising the temporal financial cost associated with today's climate action compared to the future. By failing to do so, corporations may not realise the severity of the rectification cost looming ahead. It might appear as "expensive" for the corporation to pursue a timely transition towards reducing carbon emissions today. That is perhaps a relatively small price tag in tomorrow's money. It is this dichotomy of "*spend now or spend when need be*" which has cleaved corporations asunder between shareholders and directors.

On the one hand, shareholders play an integral role in the investment put into the corporation and their returns depend on performance, which in turn depends on an appropriate strategy that accounts for factors such as climate risk. It is from this ratio that shareholders (and climate activists in general) are ever more perturbed by the lack of consideration given to climate change as reflected in the Australian case, *Nature Conservation Council of New South Wales v. Minister for Water, Property and Housing*. On the other hand, corporate directors are not always in on accepting personal or even collective responsibility for climate action, as seen in the ongoing, unlikely-to-succeed, derivative action sought in *ClientEarth v. Board of Directors of Shell* in England and Wales. Thus, how can one establish liability?

Role of Contractual Liability

The contract, as a legally binding agreement, remains at the core of international business. A non-contentious and pre-emptive starting point for corporations, worried about the legal risk of climate pledging, is to analyse and refine existing contracts, and adapt any substance that may be rendered carbon intensive. This could be anything from the commercial subject matter of the contract to the means through which the contract is delivered. For example, in a building contract context, there can be mutual obligations requiring parties to manufacture onsite as opposed to offsite, and to impose a climate remediation fee for breach. Another example is the New Engineering Contract's new 'NEC4, Option X29 Climate Change' optional clause, which impels parties to the building contract to address 'climate change requirements' via a 'Climate Change Plan' in the contractual 'Scope of Works'. Failure to comply would constitute a defect, compelling rectification by the defaulting party, akin to any other Compensation Event under the standard building contract.

The second consideration is to adapt the corporate regime to include and set out performance targets and rewards for climate compliance. These climate friendly targets would then be imparted to the corporation's internal and external contractual dealings, establishing environmental obligations leading to energy efficient ratings. These contractually reciprocated corporate targets serve as the grassroots preparatory measure for climate action, and as a precedent for forthcoming entities that will work with the corporation. By effecting these clauses, be it by way of environmental compliance officers or by way of contractual administration, a strict expectation will be established for those seeking future work opportunities. A climate premium could also be added to the contract. This would be of a trilateral essence. The climate premium would serve as: (i) a surcharge for committing to less carbon intensive operations; (ii) an insurance charge by the corporation reflecting its commitment to climate action; and, (iii) an incentivising premium that could be reaped by the contracting parties and the shareholder in the event the transaction is executed compliantly with no climate cost incurred.

Conclusion

Climate pledging has stratified from an international level to a national and a corporate level. The precipitous nature of climate litigation to enforce climate pledges is an ever-growing phenomenon. Corporations face a financial dichotomy on whether to act immediately or in the future. Corporate shareholders and directors play a direct role in effecting climate pledges and resolving the financial dichotomy. However, the boundaries of these roles are still moulding and remain uncertain. Whilst contractual liability offers a preview of how climate pledges can be effected, climate litigation will cement a concrete viewpoint of how such roles and pledges are realised. This might be achieved in the ongoing *ClientEarth v. Board of Directors of Shell* should ClientEarth succeed in its claim against Shell's directors. However, the derivative action sought by ClientEarth is unlikely to succeed per se, as there is a high threshold to exclude the rule in *Foss v. Harbottle*. The impact of climate pledges remains a matter of wait and see.