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## Climate transition plans in the EU: consistency and clarity

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### Introduction

AFME strongly supports work to create a consistent framework for high-quality transition plans for climate change mitigation across economic sectors. Transition plans provide an important tool to support the transition to Net Zero, encouraging companies to take a strategic approach to adapting their business to a low carbon economy and providing important information to investors, financial institutions and other stakeholders.

Alongside progress with transition plans, it is essential to clearly articulate transition pathways for sectors of the real economy in line with climate goals and commitments. This is necessary to enable companies to prepare effective transition plans and for banks and investors to assess them in the provision of transition finance.

A robust transition planning framework for corporates is important to enable banks to support companies in their transition through transition finance, to deliver on their own net zero commitments, for the purposes of banks' own disclosures (including their own transition plans) and to aid the assessment and management of climate risk.

AFME supports efforts to create a consistent framework for high quality transition plans across economic sectors, including the work at international level. Greater standardisation of the transition planning framework should also help companies provide the information required by financial institutions and enhance comparability for investors.

While we welcome progress in the EU and internationally on the development of a framework for transition planning, it is essential that this framework is clear, consistent and effective.

This short paper highlights different areas of proposed EU regulation on transition plans and emphasises the importance of (1) ensuring a coherent, clear framework for companies and financial institutions in the EU; and (2) ensuring international interoperability of transition planning requirements.

### Different proposals under EU regulation

There are several proposed requirements relating to transition planning currently being negotiated or finalised. These are summarised in the comparison set out in the annex and briefly highlighted below:

**CSRD/ESRS:** The European Sustainability Reporting Standards (ESRS) under the Corporate Sustainability Reporting Directive (CSRD) will include requirements for disclosure of transition plans for climate change mitigation. The draft sector-agnostic ESRS submitted by EFRAG to the European Commission include a number of disclosure requirements under ESRS E1. We understand that these provisions may be supplemented in future sectoral standards developed by EFRAG.

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**Corporate Sustainability Due Diligence Directive (CSDDD):** Article 15 of the proposed CSDDD requires Member States to ensure that companies within its scope adopt transition plans and establishes criteria which the transition plans would have to meet. These criteria differ from the ESRS and proposals under negotiation, for example in the European Parliament, would introduce different requirements to those set out in CSRD, potentially creating conflicting requirements.

**Capital Requirements Directive (CRD):** The proposed amendments to the CRD include proposals from the European Parliament to expand requirements for credit institutions to prepare transition plans. While some acknowledgment has been made of the disclosure requirements under the ESRS, again the proposed provisions differ, creating a risk of misalignment and a lack of a clear and consistent EU regulatory framework.

### **The need for coherence**

It is essential that transition planning requirements are clear and consistent across EU regulation and are established in a manner that encourages international interoperability. Definitions of transition plans need to be consistent, transition planning obligations need to be coherent with disclosure requirements and sector-specific requirements should adapt sector-agnostic requirements as appropriate, but should not create conflicting requirements.

The implementation of the ESRS will provide for widespread corporate disclosure on transition plans that is consistent across the economy. The ESRS transition plan requirements will result in disclosure on the plans of the undertaking, including implementing actions and related financial and investment plans, to ensure that its business model and strategy are compatible with the transition to a sustainable economy and with the limiting of global warming to 1,5 °C in line with the Paris Agreement. ESRS will therefore serve as an effective baseline, ensuring consistency across sectors.

It is critical that other ongoing legislative efforts do not impose additional transition plan requirements that inadvertently conflict with or create inconsistency with the ESRS, particularly given that EFRAG's sector-specific work is still ongoing and that approaches to transition planning are still in their infancy for the vast majority of companies. The proposed CSDDD and CRD legislation, however, currently have provisions that would impose transition plan requirements that are not aligned with the ESRS.

Conflicting or confusing requirements risk creating market confusion or unnecessary compliance costs that may hamper the speed and effectiveness of transition plan adoption. Transition plan requirements are intended to facilitate a smooth transition of the broader economy to net zero in line with the limiting of global warming to 1,5 °C. To achieve this goal, it is imperative that regulatory requirements focus companies and financial institutions on the most essential elements of transition planning, with clear and consistent regulatory expectations.

### **The importance of international alignment**

It is also essential to ensure that EU transition planning requirements are aligned with international standards, including voluntary initiatives, and requirements in other jurisdictions. Climate change is a global challenge and the world cannot reach net zero without addressing the transition of the broader global economy, including in jurisdictions with very different economic structures, levels of development,

and transition pathways. As different jurisdictions look to create local or regional frameworks and requirements to facilitate their transition, firms that participate in the global economy are likely to be subject to transition plan requirements in more than one jurisdiction. Given the EU's leading role in the global economy, it will be essential that firms operating in the EU are not subject to conflicting requirements in other jurisdictions. Fragmentation of transition plan requirements could undermine the objective of facilitating a timely and orderly transition.

Given that many other jurisdictions are expected to adopt the International Sustainability Standards Board (ISSB) climate disclosure standard, achieving interoperability and consistency with the ISSB's disclosure provisions on transition plans will be important to drive an internationally consistent approach to transition plans. Not only will this ease compliance for firms operating in multiple jurisdictions, but more importantly it will ensure a consistent global approach in recognition of the global nature of the transition that needs to happen.

We appreciate the work that EFRAG has done to drive interoperability with the ISSB's transition plan disclosure provisions, given that many other jurisdictions are expected to adopt ISSB-aligned disclosure requirements. Interoperability of transition planning disclosure should also help companies provide the information required by financial institutions and enhance comparability for investors.

Introducing a proliferation of separate legislative provisions also relating to transition plans risks undermining that clarity. In fact, a lack of a cohesive approach across different legislative files could inadvertently undermine both the effectiveness of the ESRS and the ability of companies to quickly adopt credible transition plans that take into account what is needed for global companies operating across jurisdictions to effectively transition.

It is important that an internationally consistent approach is taken to transition plans, including for financial institutions. Many companies and financial institutions have significant international businesses and if there is insufficient consistency and coordination of approaches there is a risk that companies are subject to multiple, potentially conflicting or overlapping requirements in different jurisdictions with the same objective, particularly if requirements are introduced at entity rather than group level. This risks undermining the objectives of a clear, comparable framework. We therefore strongly encourage international coordination to agree a common approach.

### **A suggested way forward**

It is essential that the European Commission and the co-legislators ensure the consistency and coherence of transition planning disclosures and requirements for companies and financial institutions across EU regulation. It is also essential to ensure that the regulatory framework provides sufficient flexibility to accommodate evolving practice in developing credible transition plans and ensures international compatibility.

The ESRS imposes a comprehensive transition planning framework that focuses on the most important elements of a company's transition. The ESRS framework will be consistent across the economy and should be viewed as the bedrock of EU transition plan requirements. Any further legislative requirements related to transition plans should refer to the ESRS and ensure consistency across EU requirements. Importantly, the ESRS transition plan provisions are well-positioned to apply effectively to a broad swath of firms operating in a global landscape, as a result of the work that EFRAG has done to ensure that ISSB

transition plan disclosure requirements are consistent with the ESRS requirements. This global consistency is imperative to ensure that transition plan requirements facilitate a rapid and orderly transition rather than inadvertently undermining transition objectives.

### **About AFME**

*The Association for Financial Markets in Europe (AFME) represents a broad array of European and global participants in the wholesale financial markets. Its members comprise pan-EU and global banks as well as key regional banks, brokers, law firms, investors and other financial market participants. We advocate stable, competitive, sustainable European financial markets that support economic growth and benefit society.*

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