EC – Proposal for a Directive on Corporate Sustainability Due Diligence

Human rights and environmental impacts

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1 Executive summary

General overview of the Due Diligence Directive

This Directive lays down common rules within the EU on the obligations for companies regarding actual and potential human rights and environmental adverse impacts and on liability for violations of these obligations

Companies in scope(1)

- **Group 1** → Companies with > 500 employees and > EUR 150 million in net turnover worldwide.
- **Group 2** → Companies operating in defined high impact sectors[3], which do not meet both Group 1 thresholds, but have > 250 employees and a net turnover of > EUR 40 million provided that at least 50% of this net turnover was generated in one or more of those high- impact sectors.

Perimeter

- Obligations for companies regarding actual and potential **human rights** adverse impacts and actual and potential **environmental** adverse impacts[4] , with respect to **own operations** and operations of their **subsidiaries, and the value chain operations**[5] carried out by entities with whom the company has an **established business relationship**[6].
- **Liability for violations** of the obligations.

Next steps

- EP and the Council to approve.
- Once adopted, Member States will have **2 years to transpose it** into national law and communicate the relevant texts to the EC[2].

Subject matter of this directive

Objectives of the Directive[7]

- a — Achieve a better **integration of risk management** and **mitigation in the corporate governance practices**
- b — Increase corporate **accountability for adverse impacts** and ensure coherence on **responsible business conduct**
- c — **Improve access to remedies for those affected by human rights and environmental impacts**

Due Diligence Guidance

Most of these objectives correspond to the different actions which companies shall carry out, in order to conduct human rights and environmental due diligence. These actions are explained in the following slides

1. Integrating due diligence into their **policies**
2. Identifying actual or potential **adverse impacts**
3. **Preventing, mitigating** and **bringing** potential adverse impacts to an end
4. **Monitoring the effectiveness** of their due diligence policy and measures
5. **Publicly communicating** on due diligence
6. Establishing and maintaining a **complaints procedure**

(1) This Directive also applies to Non-EU companies active in the EU with turnover threshold aligned with Group 1 and 2, generated in the EU
(2) For group 2 companies, rules will start to apply 2 years later than for group 1.
(3), (5),(6) For more information see the Annex I
(4) Adverse environmental and human impacts are specified in the Annex, Part I and II of this Directive
(7). The Directive also sets another objective to complement **other measures in force or proposed,** which directly address some **specific sustainability challenges.** For more information see the Annex II.

Access the entire Document

2 Integrating due diligence into policies

Due diligence policy

Companies shall have in place a due diligence policy that contains a set of aspects. Also, companies need to have a plan to ensure that their business strategy is compatible with limiting global warming to 1.5 °C

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Content of the due diligence policy

1. A **description** of the company's approach, including in the long term, to conduct due diligence.
2. A **code of conduct** describing rules and principles to be followed by the company's employees and subsidiaries in order to improve human rights and environmental factor inside the company. The code of conduct should **apply in all relevant corporate functions and operations**, including procurement and purchasing decisions
3. A description of the **processes** put in place to implement due diligence, including the measures taken to verify compliance with the code of conduct and to extend its application to established business relationships.

Companies shall update their due diligence policy annually.

Plan for combating climate change

1. This plan shall identify, on the basis of information reasonably available to the company, the **extent to which climate change is a risk** for, **or an impact** of, the **company's operations.**
2. In case climate change is or should have been identified as a principal risk for, or a principal impact of, the company's operations, the company includes **emission reduction objectives**.

Implications for Directors

- Directors must put in place and overseeing the due diligence actions and in particular, the due diligence policy.

- The plan should be duly taken into account when setting **directors' variable remuneration**, if variable remuneration is linked to the contribution of a director to the company's business strategy and long-term interests and sustainability.

Measures against adverse impacts
Identifying, preventing, mitigating and bringing to an end

Companies shall identify actual and potential adverse impacts arising from their own operations or those of their subsidiaries, to prevent them and make every effort to eliminate them

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1- Identifying adverse impacts

1.A- Preventing and, if is not possible, mitigate potential adverse impacts

1.B - Bringing actual adverse impacts to an end and, if it is not possible, minimize their exten.

Main sources:

- Independent reports
- Information gathered through the complaints
- Consultations with potentially affected groups

Financial undertakings: shall carry out the identification of adverse impacts before providing the financial services

Main actions for processes A and B:

- Prevention action plan
- Seek contractual assurance[1]
- Necessary investments
- Support for SMEs
- Collaborate with other entities

Main actions only for processes B:

- Neutralization measures
- Corrective action plan

Are these actions enough?

N → Conclude a contract with a partner with whom it has an indirect relationship (verification measures would apply) → Are these actions enough?

- N → Temporarily suspend commercial relations / Terminate the business relationship
- Y → Prevention or mitigation achieved

Y → Prevention or mitigation achieved

This shall not be required when is referred to financial services and can cause a substantial prejudice to the entity to whom that service is being provided

(1) From a business partner with whom it has a direct business relationship that it will ensure compliance with the company's code of conduct including by seeking corresponding contractual assurances from its partners, to the extent that their activities are part of the company's value chain (contractual cascading). When such contractual assurances are obtained, shall be accompanied by the appropriate measures to verify compliance.

Monitoring and publicly communicating

Supervision, monitoring and disclosure

For conducting appropriate due diligence, companies shall monitor the effectiveness of the taken measures and communicate publicly on their due diligence. In order to ensure these, supervisory rules have been laid down

Monitoring

- **Periodic assessments (at least every 12m)**, qualitative and quantitative, of **own operations** and measures, those of **subsidiaries** and, where related to the **value chains** of the company, those of their established business relationships, to monitor the effectiveness of the **identification, prevention, mitigation, bringing to an end and minimization** of the extent of human rights and environmental adverse impacts.
- The **due diligence policy shall be updated** in accordance with the outcome of those assessments.

Disclosure

NFRD companies?	Non-NFRD companies?
• Non-financial disclosure statement.	• Publication on their website of an **annual statement**[1] in a language customary in the sphere of international business. • The statement shall be published **by 30 April each year**, covering the previous calendar year.

(1) This obligation should be analysed in line with other complementary legislation in force.

5 Complaints procedure and company civil liability
Main characteristics

Companies shall establish complaints procedure to hear cases from potentially affected persons or its representatives. Also, companies shall be liable for damages caused by adverse impact that could have not been prevented, mitigated or brought to an end

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COMPANY COMPLAINTS PROCEDURE

Who can submit complaints

- **Persons** who are **affected** or have a reasonable grounds to believe that they might be affected by an adverse impact.
- **Trade unions** and other **worker's representatives** representing individuals working in the value chain concerned.
- **Civil society organizations** active in the areas related to the value chain concerned.

How to deal with complaints

- Establishing a procedure for **dealing with these complaints** (founded and unfounded) and inform the relevant workers and trade unions of those procedures. W**here the complaint is well-founded**, the adverse impact that is the subject matter of the complaint is deemed to be identified.

Complainants' rights

- Requesting **appropriate follow-up on the complaint** from the company with which they have filed a complaint.
- Meeting the **company's representatives** at an appropriate level **to discuss potential** or **actual** severe adverse **impacts** that are the subject matter of the complaint.

COMPANY CIVIL LIABILITY

When companies **fail to achieve the objectives of preventing** potential adverse impacts, adequately **mitigated** or **bring adverse impacts to an end** they shall be **liable for damages**.

- When a company has **sought contractual assurances** from their business partner, and they are accompanied by the appropriate measures to verify compliance, that company **shall not be liable for damages** caused by an adverse impact arising as a result of the activities of an indirect partner with whom it has an established business relationship.
- The civil liability of a company shall be without prejudice to the one of its subsidiaries or business partners.

Annex I

Definitions in relation to the perimeter and companies in scope

Definitions of high impact sectors, value chain and established business relationship, will help to better understand the perimeter and the companies in scope of this Directive

High impact sectors	The **manufacture** of textiles, leather and related products (including footwear), and the wholesale trade of textiles, clothing and foot. **Agriculture, forestry, fisheries** (including aquaculture), the manufacture of food products, and the wholesale trade of agricultural raw materials, live animals, wood, food, and beverages. The **extraction of mineral resources** regardless from where they are extracted (including crude petroleum, natural gas, coal, lignite, metals and metal ores, as well as all other, non-metallic minerals and quarry products), the **manufacture of basic metal products**, other non-metallic mineral products and fabricated metal products (except machinery and equipment), and the wholesale trade of mineral resources, basic and intermediate mineral products (including metals and metal ores, construction materials, fuels, chemicals and other intermediate products).
Value chain general concept	The value chain should **cover activities related to the production of a good or 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 established business relationships** of the company. It should encompass **upstream established direct and indirect business relationships** that design, extract, manufacture, transport, store and supply raw material, products, parts of products, or provide services to the company that are necessary to carry out the company's activities, and also **downstream relationships**, including **established direct and indirect business relationships**, that use or receive products, parts of products or services from the company up to the end of life of the product, including inter alia the distribution of the product to retailers, the transport and storage of the product, dismantling of the product, its recycling, composting or landfilling.
Value chain concept regarding financial undertakings[1]	Provision of such services should be **limited to the activities of the clients** receiving such services, and the **subsidiaries** thereof whose activities are linked to the contract in question. **Clients that are households and natural persons not acting in a professional or business capacity**, as well as small and medium sized undertakings, should **not be considered** to be part of the value chain. The **activities of the companies or other legal entities that are included in the value chain of that client** should **not be covered**.
Established business relationships	A **business relationship**, whether **direct or indirect**, 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.

(1) **Providing loan, credit, or other financial services**

Annex II
Related normative

The new directive will affect entities already impacted by NFRD, CSRD, SFDR and Taxonomy Regulation and will complement them

Previous regulation	New Directive on corporate sustainability due diligence
1 **Non-Financial Reporting Directive (NFDR)**[1] requires certain large companies to disclose information related to: • Environmental matters • Social matters and treatment of employees • Respect for human rights • Anti-corruption and bribery • Diversity on company boards (in terms of age, gender, educational and professional background). 2 The proposal on a **Corporate Sustainability Reporting Directive (CSRD)**[2] extends the scope of the companies covered by NFRD to all large and all listed companies (except listed microcompanies).	✓ Complements the current NFRD and proposal for CSRD by adding a **substantive corporate duty** for some companies to **perform due diligence** to identify, prevent, mitigate and account for external harm resulting from adverse human rights and environmental impacts in the company's own operations, its subsidiaries and in the value chain. ✓ Thus, this Directive will lead to **companies' reporting being more complete and effective**. Therefore, complementarity will increase effectiveness of both measures and drive corporate behavioural change for those companies
3 **The Sustainable Finance Disclosure Regulation (SFDR)**[3] introduces **disclosure requirements for sustainability-related information to financial firms selling investment products and financial advisers.**	✓ This Directive will also underpin the SFDR, as the undertakings under its scope are required to **publish**, among others, **a statement on their due diligence policies** with respect to principal adverse impacts of their investment decisions on sustainability factors on a comply or explain basis.
4 The **EU Taxonomy Regulation**[4] for sustainable activities consists of a transparency tool that facilitates decisions on investment and helps tackle greenwashing by providing a **categorization of environmentally sustainable investments in economic activities that also meet a minimum social safeguard**.	✓ Complements the Taxonomy Regulation as it has the potential to further **help investors to allocate capital to responsible and sustainable companies**.

(1) NFRD applies from January 2017; (2) CSRD is expected to apply from January 2023; (3) SFDR applies from 10 Mach 2021; (4) The EU Taxonomy applies from January 2022.

Abbreviations

Abbreviation	Meaning
CSRD	Corporate Sustainability Reporting Directive
EC	European Commission
EU	European Union
NFRD	Non-Financial Reporting Directive
OECD	Organisation for Economic Co-operation and Development
SFRD	Sustainable Finance Disclosure Regulation
SME	Small and Medium Enterprise
UCITS	Undertakings for the Collective Investment of Transferable Securities

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