

## Corporate due diligence and corporate accountability - Legislative development in the European Union

Latest update: 17 December 2020

### Initial commitment at EU level

*"[T]here is a clear risk that human rights are not respected everywhere. We can only respond to all these challenges by upgrading our unique social market economy in order to achieve a more equal, inclusive and environmentally sustainable model. [...] In the present crisis, we realised how important it is for the businesses themselves to properly integrate the interests of the society in which they operate, of the workers and those depending on the companies for their sheer survival and sustainability."*

*Didier Reynders, EU Commissioner for Justice – April 2020*

EU Commissioner for Justice, Didier Reynders, announced in April 2020 his commitment to a legislation on corporate mandatory human rights and environmental due diligence in 2021. Such initiative was welcomed by many stakeholders<sup>1</sup> and member States, including Germany, which held the presidency of the EU Council in the second half of 2020 and was pushing towards a European solution. On 1 December 2020, the EU Council, i.e. the member states' governments, unanimously agreed that the European Commission shall move forward and propose a "legal framework on sustainable corporate governance, including cross-sector corporate due diligence obligations along global supply chains."<sup>2</sup> The regulatory initiative is planned to be tabled in the second quarter of 2021.<sup>3</sup>

This development reflects many stakeholders' expectations towards businesses. The media and civil society reveal human rights abuses by companies and campaign for remediation,<sup>4</sup> NGOs rate companies according to their human rights performance,<sup>5</sup> investors increasingly consider labour and

<sup>1</sup> On 2 September 2020, 26 companies, business associations, and initiatives called for an EU-wide, cross-sectoral mandatory human rights and environmental due diligence legislation in a joint statement. On 23 June 2020, 45 civil society organisations congratulated Didier Reynders for his commitment, underlined the necessity and emphasized key aspects the legislation should include in an open letter. On 21 April 2020, a group of 101 international investors representing over USD 4.2 trillion in assets under management made a general call to lawmakers to put in place regulatory measures for mandatory human rights due diligence.

The Business & Human Rights Resource Center has compiled a detailed list of companies that support human rights due diligence legislations at EU level and at national level.

<sup>2</sup> European Council: Human rights and decent work in global supply chains: the Council approves conclusions

<sup>3</sup> European Commission: Sustainable corporate governance

<sup>4</sup> For instance, after the collapse of a garment fabric that Benetton was sourcing from, Benetton was pressured by the media and an online petition and agreed to pay 1.1 million USD into the "Rana Plaza Fund".

<sup>5</sup> See, for instance, Oxfam's Supermarket Scorecard, BankTrack's evaluation of banks' human rights management processes, and the Corporate Human Rights Benchmark.

human rights issues in their investment decisions,<sup>6</sup> consumers take into account social criteria in their buying behaviour,<sup>7</sup> and a company's talent attraction also depends on its take on social aspects.<sup>8</sup>

The regulatory commitment at EU level also mirrors well the legislative trends in different European countries. Current regulations include human rights due diligence processes (e.g. Loi relative au devoir de vigilance in France or the Child Labour Due Diligence Law) or transparent reporting on how human rights issues are managed (e.g. UK Modern Slavery Act). There are a number of current legislative initiatives at various stages of the political process in other European countries, such as Norway, Sweden, Denmark, Luxembourg, Belgium, Italy and Austria.<sup>9</sup>

This trend at national levels is coupled with a general trend also at the EU level to foster responsible business conducts. Financial market participants already have the obligation to report on their human rights due diligence efforts, including on human rights topics.<sup>10</sup> Finally, the entry into full force in 2021 of the EU Conflict Minerals Regulation will require supply chain due diligence obligations for Union importers of tin, tantalum and tungsten, their ores, and gold originating from conflict-affected and high-risk areas.<sup>11</sup>

The legislative initiative on mandatory human rights and environmental due diligence is planned to be launched in 2021 and is to be seen as part of the European Green Deal<sup>12</sup> and the European Recovery Plan<sup>13</sup>. Calls have been made by civil society organisations and during high-level webinars to align the upcoming legislation with the revised EU Non-financial Reporting Directive<sup>14</sup> (NFRD) and the EU Sustainable Finance Taxonomy within the Sustainable Finance Action Plan.<sup>15</sup>

The aim of a legislation at EU level is to **create a level playing field for companies** that operate in the EU market. Furthermore, it intends to **provide legal clarity and certainty. Effective enforcement** and

<sup>6</sup> See, for instance the study on the German, Austrian and Swiss sustainable finance markets by the [Forum Nachhaltige Geldanlagen](#), and Larry Fink's (Chairman and CEO of BlackRock, the world's largest asset manager) [letter to CEOs](#).

<sup>7</sup> Capgemini finds in its [report](#) that 79% of consumers change their consumption behaviour due to the social and environmental impact of their purchases and that 53% of consumers would switch to lesser known brands if they felt their product was more sustainable.

<sup>8</sup> See Deloitte's annual [millennial studies](#).

<sup>9</sup> The Business & Human Rights Resource Center offers an [overview of national and regional movements in Europe](#).

<sup>10</sup> See our [paper](#) 'Are you complying with the EU Sustainability-Related Disclosures Regulation?' Find the legislative text [here](#).

<sup>11</sup> Find more information on the EU Conflict Minerals Regulation [here](#).

<sup>12</sup> The [European Green Deal](#) commits to place all of the EU's activities and policies under environmental objectives in order to transform its economy and lead its society to a more sustainable path. It is an integral part of the Commission's strategy to implement the [Sustainable Development Goals](#) (SDGs) by 2030. Human rights are at the center of the SDGs. Thus, a human rights and environmental due diligence will be crucial to achieve these goals.

<sup>13</sup> The [European Recovery Plan](#) is a plan to 'help repair the economic and social damage brought by the coronavirus pandemic, kick-start European recovery, and protect and create jobs'.

<sup>14</sup> The NFRD is currently under revision. The target date for the review has been set to the first quarter of 2021. More information [here](#) and [here](#).

<sup>15</sup> The [EU Sustainable Finance Taxonomy](#), developed in the context of the Sustainable Finance Action Plan, explicitly requires financial products to fulfill [minimum safeguards](#), which include a human rights due diligence, in order to be eligible to be called environmentally sustainable under the EU Taxonomy. The European Parliament called in May 2018 on the Commission in its [Sustainable Finance Action Plan](#) that the sustainability taxonomy should be complemented by a legislative proposal on 'an overarching, mandatory due diligence framework including a duty of care to be fully phased-in within a transitional period and taking into account the proportionality principle'.

an **improved access to remedy** is one of the main benefits of the law for those affected by human rights violations.

### Where are we now?

The European Parliament's Committee on Legal Affairs issued in September 2020 a draft report for adoption by the Parliament. The draft includes recommendations to the European Commission for a Directive on corporate due diligence and corporate accountability for the sake of "harmonization, legal certainty and the securing of level playing field".<sup>16</sup>

*What do we already know about the content of the proposed Directive?*

According to the Committee, the Directive should include the **following main elements**:

- **Far-reaching scope** – the Directive should apply to "all undertakings governed by the law of a Member State or established in the territory of the Union"<sup>17</sup>, irrespective of their size or sector and of whether they are publicly owned or controlled undertakings. It should also apply to undertakings governed by the law of a non-Member State and not established in the EU when they sell goods or provide services in the EU.
- **Due diligence strategy on human rights, environmental and governance risks** – Undertakings should have a due diligence process in place with respect to human rights (incl. social and labour rights), the environment (incl. through climate change) and governance risks in their own operations and business relationship. This includes an assessment on whether its operations and business relationships cause or contribute to any such risks, and the consequent establishment of a due diligence strategy in order to cease, prevent or mitigate those risks.
- The **due diligence should encompass the entire value chain**, incl. company's own activities or of those of its business relationships. The value chain due diligence should be proportionate and commensurate to the undertaking's specific circumstances, sector, size and length of its supply chain, capacity, resources and leverage. This implies that small, medium-sized and micro enterprises (SMEs) may need less extensive and formalised due diligence processes.
- **Involvement of trade unions and consultation of stakeholders** – Undertakings should carry out effective, meaningful and informed consultations with trade unions and stakeholders (such as affected or potentially affected stakeholders, indigenous peoples or workers) when establishing and implementing their due diligence strategy.

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<sup>16</sup> Para 9 of the *Annex to the motion for a resolution: recommendations as to the content of the proposals requested in the draft report*.

<sup>17</sup> Article 2 of the proposed Directive as an Annex in the draft report.

- **Grievance mechanism** - Undertakings should establish a grievance mechanism in line with the UN Guiding Principles<sup>18</sup> (UNGPs). It should serve both as an early-warning risk- awareness and as a remediation system, allowing anyone to raise concerns regarding the existence of a human rights, environmental or governance risks.
- **Responsibility with regards to the due diligence process** – Members of the administrative, management and supervisory bodies of an undertaking are responsible for ensuring the adoption and implementation of the due diligence process. Large undertakings should have an **advisory committee** with expertise on due diligence matters the undertaking should benefit from.
- **Sectoral due diligence plans** – Member States should encourage the adoption of sectoral due diligence action plans to enhance consistency and effectiveness, including sectoral grievance mechanisms.
- **Small, medium-sized and micro enterprises (SMEs)** – Member States shall make available a specific portal for SMEs. Furthermore, SMEs shall be eligible for financial support to perform their due diligence obligations and specific guidelines for SMEs shall be published.
- **Enforcement** – Member States should designate one or more national authorities to supervise the correct implementation by undertakings of their due diligence obligations. They should be entitled to conduct appropriate checks and **impose penalties**, a repeated infringement of the relevant national provisions in accordance with the Directive constitutes a criminal offence.

## What's next?

The Legal Affairs Committee of the European Parliament has requested the European Commission to follow the recommendations and submit a legislative proposal on mandatory due diligence without undue delay. Two other parliamentary committees have already commented on the draft and are in favor of a legislation.<sup>19</sup>

The Commission launched a **public consultation on the new due diligence legislation on 26 October 2020** to gain input from different stakeholders on how to draft their proposal. The feedback period runs until 8 February 2021.<sup>20</sup> This consultation addresses, among others, the extent of corporate directors' responsibility to address actual and potential adverse human rights, social, health and environmental impacts on stakeholders in the company's own operations and in the company's the

<sup>18</sup> [The United Nations Guiding Principles on Business and Human Rights](#)

<sup>19</sup> For more information on draft opinions, please click [here](#)

<sup>20</sup> Find the public consultation [here](#).

supply chain; how the due diligence duty should be enforced; and how the burden on smaller companies should be reduced.

Once the European Commission submits its legislative proposal, it will be considered and voted on by the EU Parliament and the European Council. If adopted, the legislation will be a **Directive**, meaning that Member States need to transpose the Directive into national law generally within 2 years after the Directive comes into force.

### What to expect for businesses?

Although this proposal is yet to be discussed and revised, such initiative is part of a growing trend towards mandatory due diligence – **companies that already have a robust human rights due diligence aligned with the UNGPs will certainly be in greater shape to comply with such legislative proposal.**