

1. Procedural information

# Lead DG, Decide Planning/CWP references

This Staff Working Document was prepared by the Directorate-General for Justice and Consumers (DG JUST) and DG Internal Market, Industry, Entrepreneurship and SMEs.

The Decide reference of this initiative is PLAN/2019/5404 Proposal for legislation fostering more sustainable corporate governance in companies.

This initiative is identified under number 15 in Annex I of the [Commission Work Programme 2021](https://eur-lex.europa.eu/resource.html?uri=cellar%3A91ce5c0f-12b6-11eb-9a54-01aa75ed71a1.0001.02/DOC_2&format=PDF), under the heading “An Economy that Works for People”.

# Organisation and timing

An Inter Service Steering Group (ISSG) was established to support the work of DG JUST.

DGs and services participating in this ISSG are: AGRI, CLIMA, COMM, COMP, EEAS, EMPL, ENER, ENV, FISMA, FPI, INTPA, JRC, MARE, SANTE, SG, SJ, TRADE.

The ISSG has held 4 meetings (08/09/2020, 11/12/2020, 01/02/2021 and 15/03/2021). DG JUST consulted the ISSG on all the different steps of this initiative: Consultation strategy, Open Public Consultation questionnaire and the draft Impact Assessment report.

A written consultation of the ISSG has been conducted on the revised draft Impact Assessment report end of October 2021.

Publication on EUROPA website of the Roadmap on the initiative, 30 July 2020.

Open Public Consultation, 26 October 2020 - 8 February 2021 (14 weeks).

# Consultation of the RSB

An upstream meeting was held with the Regulatory Scrutiny Board (RSB) on 13 January 2021 to informally discuss questions concerning how to prepare the best possible report for this initiative. The IA report was submitted to the RSB on 9 April 2021 with a subsequent RSB hearing scheduled on 5 May 2021. The RSB provided a negative opinion on 7 May 2021. Taking into account the RSB comments, a revised Impact Assessment report was resubmitted on 5 November 2021.

| General RSB Comments | How the general RSB comments have been addressed in the IA |
| --- | --- |
| (1) The problem description is vague and does not demonstrate the magnitude and likely evolution of the problem. It does not provide clear evidence that EU business (including SMEs) do not sufficiently address sustainability opportunities, risks and impacts. | The Impact Assessment report has been revised, shortened and streamlined following the RSB’s Opinion and Impact Assessment Quality Checklist, improving its presentation as well as its content.  The problem definition has been amended to set out more concretely which problems the initiative intends to tackle. The new version of the report elaborates on the magnitude of the problem, and its likely evolution. It provides concrete evidence that EU businesses, including – based on a new Commission study - SMEs, do not sufficiently address sustainability opportunities, risks and impacts (see sub-problems 1 and 2 Sections 2.1.2 and 2.1.3) as well as under 2.2 and additional evidence provided in Annex 10. |
| (2) The policy options are too limited and do not adequately reflect the available policy choices in terms of company and sector scope, content of measures and range of delivery instruments. The added value and likely effectiveness of several of the measures are unclear. | The new version of the report presents a broader and more nuanced range of policy options varying in terms of companies in the scope, content of the duties regarding both directors’ duties and due diligence, industry sectors covered, sustainability concerns covered, delivery instrument, etc. (see Section 5.2). |
| (3) The assessment of proportionality is insufficient. Costs and benefits are not sufficiently presented. | Option have been revised to ensure more proportionality. Furthermore, the new version of the report presents a detailed assessment of the proportionality of the policy options assessed (see Sections 6.1.9, 6.2.9, 6.3.6)The cost and benefit assessment has been revised and has been elaborated on in more detail. |
| (4) The report does not sufficiently integrate differentiated stakeholder views. | The new version of the report presents views as per stakeholder groups (Annex 2, and elsewhere in the text) and integrates differentiated stakeholder views in the problem definition and when discussing options and impacts (Sections 2.2, 3.2, 6 (specifically 6.1.7, 6.2.4, 6.3.6), and elsewhere in the text). |

| Specific RSB Comments | How the specific RSB comments have been addressed in the IA |
| --- | --- |
| (1) The problem definition sets out a very broad and intangible problem. The claimed insufficient sustainability practices in companies concerns a wide range of climate, environmental, human rights, social and health related issues and their internal and external impacts. The report should clarify what problem this initiative aims to tackle and why it is not sufficiently covered by existing or planned sectoral and horizontal legislation or private sector initiatives. The report should clarify if the problem concerns insufficient sustainable governance in the interest of the company, or companies breaching sustainability and human rights standards. It should describe the magnitude of the problem and how it will evolve, taking into account expected market and societal dynamics. It should clearly establish why the problem cannot be tackled appropriately at the level of Member States. | As explained above, the problem definition (Section 2) has been amended to set out more concretely which problems precisely the initiative intends to tackle and which sustainability issues it intends to address (see sub-problems 1 and 2 Sections 2.1.2 and 2.1.3).  The report explains more in detail   * why it is not sufficiently covered by existing or planned sectoral and horizontal legislation or private sector initiatives (see Section 1.2.2, the Baseline in Section 5.1). Annex 7 contains a detailed mapping about existing EU initiatives or those in the pipeline and provides explanations about the added value of the sustainable corporate governance initiative. * that the problem concerns both insufficient sustainable governance in company’s own operations, **and** companies obligation to perform due diligence regarding risks in their value chains breaching human rights standards and sustainability (see explanation in Section 2.1.1); * the magnitude of the two aspects of the problem and how they will evolve, taking into account expected market and societal dynamics (see Section 2.3); * why the problem cannot be tackled at Member State level (Section 3). |
| (2) The report is not clear about why existing sustainability strategies and corporate management practices are considered as insufficient or what in practice companies would have to do to have adequate sustainability governance practices in place. It should substantiate with clear evidence that EU business (including SMEs) do not sufficiently address sustainability opportunities, risks and impacts via their corporate management systems. | The revised report clarifies with evidence why existing sustainability strategies and corporate management practices are insufficient, it provides clear evidence on the reasons why EU businesses, including –based on a new Commission study - SMEs do not sufficiently address sustainability matters via their corporate management systems (see sub-problems 1 and 2 Sections 2.1.2 and 2.1.3 as well as under 2.2 and additional evidence provided in Annex 10). |
| (3) The report argues that the problems pertain to more or less all companies independent of their size (all above 20 employees) or sector. What is the risk that SMEs are engaged in unsustainable practices? What is the evidence that companies (particularly SMEs) in all sectors will have the market power to generate real change on the ground through processes of due diligence and directors’ duties? | The new version of the report examines practices at the level of SMEs and provides evidence that the problems also pertain to SMEs (see sub-problems 1 and 2 Sections 2.1.2 and 2.1.3 as well as under 2.2 and additional evidence provided in Annex 10). However, as to SMEs, regulatory options regarding due diligence have been limited to cover only medium-sized companies operating in high impact sectors and listed SMEs in some options. Based on existing international standards and frameworks, due diligence is not dependent on the company exercising market power. Possibilities to generate change can be increased by building leverage in the value chain, for example through the company’s cooperation efforts with other companies sourcing from the same supplier, etc. Under directors’ duties, only the general duty would apply to all SMEs. |
| (4) The policy options are too limited and do not sufficiently reflect the available policy choices. Given the sensitive nature of corporate governance, the radical change of approach from existing practise, the uncertainty in terms of effectiveness and efficiency, and potential subsidiarity issues, the policy options should offer a broader and more nuanced range of options allowing for more diverse policy packages, with measures including different levels of ambition, scope and legal obligations. Soft law instruments should be assessed in a more nuanced and balanced way, and be considered in possible combination with selected hard law elements. The need for transitional measures, including experimental or adaptive approaches should be considered. | The new version of the report expanded the policy options with more differing options in terms of their level of ambition. It presents a broader and more nuanced range varying in terms of size of companies in the scope, content of the directors` duties and due diligence, industry sectors covered, enforcement, sustainability risks covered (see Section 5.2).  The report also assesses soft law instruments in more detail and considers possible combinations with hard law instruments. The report also considers sector-by-sector approaches and phasing in of obligations for certain companies (see Options section as well as detailed description of Options in Annex 13). |
| (5) Overall, the options should provide more clarity on the content, added value and effectiveness of elements included such as due diligence, target setting at company level, directors’ nominations or the role of competent authorities. The report should also clearly set out the added value of a very broad horizontal due diligence regime compared to sectoral approaches focusing on clearly identified shortcomings. | The new version of the report clarifies more in detail the content of the specific duties, where relevant, including in Annex 13 on the detailed description of the duties and of the Options. The initiative does not aim at regulating directors’ nominations. Overall, the text elaborates in detail on the added value of the different measures and their effectiveness, including as regards due diligence, target setting at company level, or the role of competent authorities. Annex 7 includes detailed mapping of the added value of the instrument compared to existing EU measures or those in the pipeline, and explains the relationship with other sector specific instruments.  It also expands on the added value of the horizontal approach compared to a sectoral approach (Section 6.1.1.). |
| (6) The report should clarify how third country businesses would be covered by the initiative and how effective enforcement would be ensured in view of global level-playing field concerns. It should clarify what standards would apply to third country companies in the value chain and how these would be aligned with international agreements, such as the Paris Agreement. | The new version of the report goes in much more detail on how third country businesses would be covered by the initiative and how effective enforcement would be ensured (Section 5.2.1.3, **Annex 13**). It also clarifies how third country companies in the value chain of EU companies would be affected by the due diligence duty and how the duty would be aligned with international agreements, such as the Paris agreement. |
| (7) A more consistent intervention logic should be established, based on a clearer problem definition, specific objectives expressed in SMARTer terms and a clearer link to a wider range of policy options. Costs, benefits, trade-offs, and proportionality of options should be brought out more clearly. | The intervention logic has been revised and adapted to a clearer problem definition. Specific objectives have been defined in SMARTer terms, mirroring the problem drivers.  Costs, benefits, trade-offs, and proportionality of options are brought out more clearly. |
| (8) The report should include a more nuanced assessment of impacts on companies, notably SMEs, innovation and competitiveness. It should assess how this initiative impacts on the fundamental rights to conduct a business and on property and ownership rights. Moreover, the report needs to clearly distinguish between having certain practices (e.g. due diligence obligations, sustainability targets) in place and the extent to which they are effective in reaching sustainability or human rights objectives, and having a real-world impact on climate, environment and social issues. It should also convincingly show that these effects could not be reached by other legislation or voluntary corporate initiatives under the baseline. | The report includes a more nuanced assessment of impacts on companies, including on costs and benefits, based on a more detailed analysis taking all available information into account.The report presents the impacts on fundamental rights to conduct a business and on property and ownership rights. It also analyses the effectiveness of certain measures in reaching sustainability or human rights objectives, and having a real world impact on climate, environment and social issues, in particular based on the available evidence on the French law, etc.  The report demonstrates how due diligence can have a real impact on the ground and that legislation is the most efficient to mainstream good practice.  Lastly, the report shows that the desired effects could not be reached by other legislation (see added value mapping in Annex 7) or voluntary corporate initiatives (see problem definition, drivers). |
| (9) Given the uncertainty that the expected benefits will actually materialise and the substantial costs resulting from a broad set of measures that would be imposed on up to 2 million companies, the proportionality of the options needs to be significantly better argued. In particular, the inclusion of SMEs in the scope requires a more critical proportionality reflection. Subsidiarity issues also require more attention, given that many SMEs operate largely within national borders and given the national focus of company law. The comparison of options should provide a more convincing assessment of effectiveness, efficiency, coherence and proportionality. | The report demonstrates, based on available evidence, including the French law, that due diligence legislation is likely to be effective. The report does no longer propose a broad set of measures to be imposed on 2 million companies and proportionality was considered when defining the options as regards SMEs and through the indirect impacts of the initiative. Moreover, the options covering smaller companies in high-impact sectors are limited only to medium-sized companies with 50+ employees and listed SMEs in some options. The comparison of options has been revised based on the RSB detailed comments and provides a more elaborated analysis on effectiveness, efficiency, coherence and proportionality. |
| (10) The report should present the diverse stakeholder views better. This should be done in the main text (notably in the problem section and when discussing options and impacts) but also in annex 2, while more seriously addressing the criticism raised by stakeholders and academics. More generally, the report should be revised to present the evidence in a more balanced and neutral way. | Annex 2 presents the views as per stakeholder groups. The new version of the report integrates differentiated stakeholder views in the problem definition and when discussing options and impacts (Sections 2.2, 3.2, 6 (specifically 6.1.7, 6.2.4, 6.3.6), and elsewhere in the text)The views of certain academics, in particular as regards short-termism have been carefully considered and reflected on or reacted to, where necessary, as explained in the report. Evidence is presented in a balanced way. (See under drivers) |

# Evidence, sources and quality

## Studies commissioned by the European Commission

* Study on due diligence requirements through the supply chain; British Institute of International and Comparative Law, Civic Consulting, Directorate-General for Justice and Consumers (European Commission), LSE, ISBN 978-92-76-15094-7, DOI 10.2838/39830, Catalogue number DS-01-20-017-EN-N, 20-02-2020 (<https://op.europa.eu/en/publication-detail/-/publication/8ba0a8fd-4c83-11ea-b8b7-01aa75ed71a1/language-en>)

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## External Expertise

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EBA

EOIPA

ESMA

Eurostat

ILO

OECD

World Bank

World Economic Forum

WWF

1. Stakeholder consultation

# Introduction

This report is the synopsis report for all stakeholder consultation activities undertaken as part of the impact assessment. In line with the Better Regulation requirements, this report provides an outline of the consultation strategy, documents the consultation activities undertaken, presents the stakeholder groups that participated and describes the methodology and tools used to process the data gathered. The results of each consultation activity are briefly presented.

# Consultation strategy

The objective of the consultation strategy was to ensure that all relevant stakeholders are identified and are given the opportunity to take part in the consultation activities; and to gather data and stakeholder views on further embedding sustainability into the corporate governance framework.

The consultation strategy was implemented through the use of several consultation tools. This includes the inception impact assessment (roadmap) feedback, open public consultation, consultation of social partners and a number of stakeholder workshops and meetings (e.g. meeting of the informal company law expert group mainly composed of company law legal academics (ICLEG), meeting with Member State representatives in the Company law Expert Group (CLEG), meetings with business associations, individual businesses, including SMEs representatives, civil society, including non-governmental and not-for-profit organisations as well as OECD).

All the consultation activities carried out provided valuable input for the impact assessment. The information gathered through the consultation activities complemented evidence gathered from other strands (e.g. literature review) and allowed to triangulate evidence for the impact assessment.

# Inception impact assessment consultation (IIA)

The consultation period lasted from 30 July 2020 to 8 October 2020. 114 feedbacks were received, analysed and taken into account in the development of the open public consultation.

The respondents were mainly representatives of NGOs (27.7%), business associations (18.6%), companies/businesses (14.3%), followed by academic research organisations, citizens, trade unions, public authorities, consumer organisations and environmental organisations.

## Directors’ duty of care – stakeholder interests

A general assessment of the responses is that there are different opinions on the need for the Commission to act in the sphere of directors’ duties. Most business association stakeholders expressed critique toward the findings of the Supporting study on directors’ duties, and most respondents mistakenly assumed that that the Roadmap was founded solely on its conclusions. More particularly, business associations cautioned about the possible negative effects on dynamism and innovation, which require the avoidance of lock-in effects, investors’ willingness to invest which could result in reduction of foreign investment and thus a loss of competitiveness. In turn, according to this line of reasoning, uncertainty and a reduction in the shareholder surplus could negatively affect funding for the development of environmentally friendly technologies. Overall, most business associations were in favour of soft law on directors’ duties or a gradual approach, thereby allowing the effects of new legislation (SRDII, taxonomy, CSRD) to materialise before introducing new measures.

In contrast, individual businesses, many of which can be expected to have experience in integrating suitability aspects in their operations[[1]](#footnote-2), expressed overall support for the measures highlighting that economic and social progress cannot be decoupled, with some expressing preference for self-regulation on directors’ duties.

While generally not providing specific input on the directors’ duties aspects, civil society organisations agreed that the current model of corporate governance needs reform as current corporate governance practice is contributing to a wide range of systemic risks, as well as devastating social, environmental and economic impacts. Therefore, they expressed support for changes to company law that require boards of directors to develop, disclose and implement a corporate sustainability strategy including verifiable targets as well as for a specified percentage of the KPIs and remuneration of executive management to be linked to the achievement of measurable targets set in the company’s sustainability strategy.

## Due diligence duty

A general assessment of the responses is that the Commission acting in the sphere of due diligence would be very welcome. Business associations generally supported the need for an EU mandatory legal framework. They voiced preference for the measure to be based on UNGPs, OECD guidelines and ILO norms including the possibility of recognising the compliance of industry schemes. The need for common definitions was emphasized as well as the need for realistic accountability. They also stressed the need to consider the issue of global competitiveness (covering non-EU companies operating in EU), to incentivise the EU’s trading partners to improve responsible business conduct, to ensure legal certainty (clear rules) and proportionality of obligations.

Similarly, individual businesses, many of which are expected to have some due diligence processes in place[[2]](#footnote-3), expressed strong support for a mandatory EU due diligence legal framework for both human rights[[3]](#footnote-4) and environmental[[4]](#footnote-5) impacts for the purpose of creating a global level-playing field. Recommendations were given as regards the need for coordination with NFRD, adopting a risk-based approach following existing international frameworks, cross-sectorial nature applicable to all businesses, clear definitions of roles and accountabilities, a practical approach (judged on efforts) and recognition of industry schemes. As regards the reach, business relationship direct linkage was preferred considering the value chain complexity. As regards supervision, businesses were of the view that a single EU body or national bodies with strong alignment should supervise. Preference for sanctions for non-compliance was civil/administrative liability.

Civil society organisations agreed that voluntary measures have failed. They overwhelmingly supported the need for the establishment of a cross-sectoral mandatory human rights and environmental due diligence obligations for all companies, whether domiciled or otherwise operating within the EU and independent of their form or size, including stakeholder engagement, access to remedy for victims of corporate abuse and effective sanctions including liability. They considered that different rules imposed by Member States could threaten the functioning of the internal market. More particularly, as regards the substance, they called for placing right holders at the core of the process and including impacts on governance risks as part of the initiative. As regards foreseen benefits, they highlighted how effective due diligence is in the interest of companies themselves as environmental and human rights considerations can entail significant material risks for companies.

# Open public consultation (OPC)

The purpose of the consultation carried out from 26 October 2020 until 8 February 2021 was to gather views of the stakeholders on the need for and the objectives of the EU intervention as well as on the different policy options to reach these objectives and the anticipated costs and benefits of different policy options. The consultation was carried out in all official EU languages, it contained both open and closed questions. The respondents were not obliged to answer all questions. The consultation attracted a broad range of stakeholders.

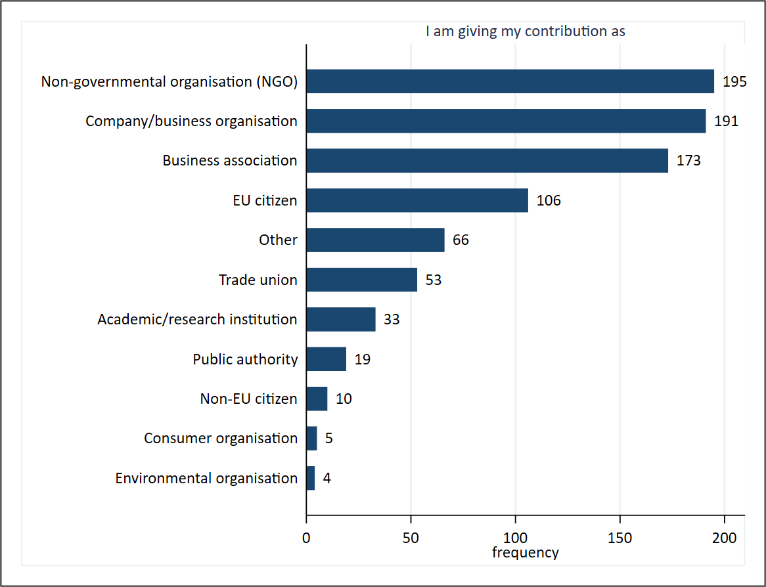
473.461 public responses were received, one of which had 122.785 supporting citizen signatures, and a total of 149 position papers.[[5]](#footnote-6) One of the responses. The high number of overall responses was driven to a large extent by campaigns carried out by a number of NGOs using pre-filled questionnaires. Of the 473.461 total responses, 472.606 responses have been identified as submitted through campaigns using a methodology known as “key-collision clustering algorithm”. Following the recommendations from the Better Regulation Toolbox[[6]](#footnote-7), these responses were segregated and analysed separately from the non-campaign responses. This avoids overall results being distorted by the large number of campaign responses.

The complete analysis followed the outset of identifying, structuring, weighing and balancing all stakeholder responses in order to ensure all stakeholder views are duly represented. E.g. association, organisations and unions representing a larger sample of respondents were recognized and appropriately treated in the analysis.

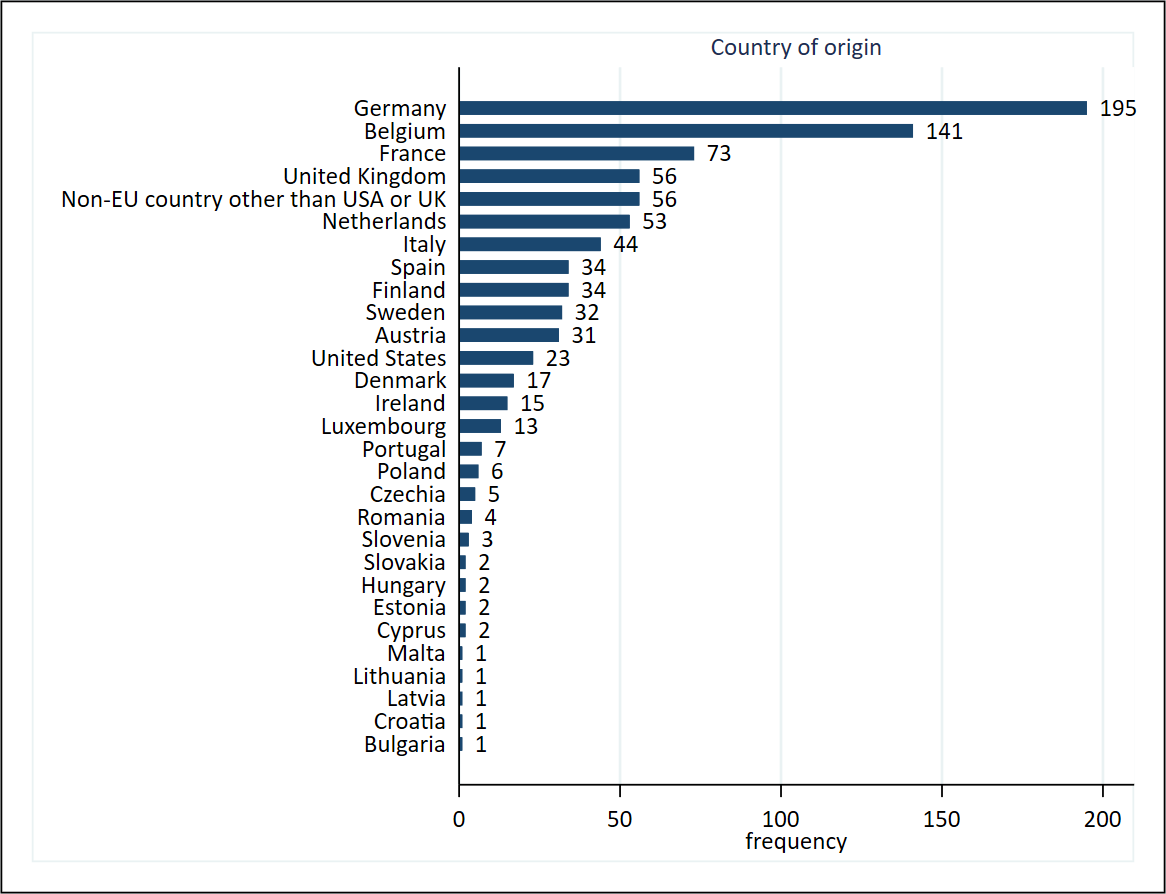
The presentation below summarizes and outlines the specificities of this analysis.

## Results of OPC – ”Have your say”

The remaining 855 respondents are further broken down presented in the figure below:[[7]](#footnote-8)



As for the geographical coverage, the replies originated from almost all the EU Member States, except Greece, as presented in the figure below:



Key points from the OPC analysis include[[8]](#footnote-9):

Need and objectives for EU intervention

* 78.2% respondents agreed[[9]](#footnote-10) that there is need for a **holistic approach** in companies and their directors taking account of stakeholder interests in corporate decisions.[[10]](#footnote-11)
* 82% of respondents agreed[[11]](#footnote-12) that an **EU legal framework** for due diligence needs to be developed.[[12]](#footnote-13)
* The top five **benefits** of an EU legal framework, listed by respondents (irrespective of their category) as important were:
  + Harmonisation to avoid fragmentation in the EU;
  + Ensuring that a company is aware of its adverse human rights, social and environmental impacts and that it is in a better position to mitigate these risks and impacts;
  + An effective contribution to a more sustainable development, including in non-EU countries;
  + Levelling the playing field;
  + Increasing legal certainty about how companies should tackle their impacts, including in their value chain.
* The **drawbacks** of an EU legal framework considered most important are:
  + Increased administrative costs and procedural burden;
  + Competitive disadvantage vis-à-vis third country companies not subject to a similar duty;
  + Penalisation of smaller companies with fewer resources;
  + Disengagement from risky markets, which might be detrimental for local economies.

Directors’ duty of care – stakeholder interests

* 70% of respondents believe corporate directors should be required by law to a) **identify the company’s stakeholders and their interests**, b) **manage the risks for the company in relation to stakeholders** and their interests and c) **identify opportunities** arising from promoting stakeholders’ interests .[[13]](#footnote-14)
* 70 % of respondents believe that corporate directors should set up **adequate procedures and measurable (science-based) targets** to ensure impacts on stakeholders are identified, prevented and addressed.[[14]](#footnote-15)
* 68% of respondents believe that corporate directors should **balance the** **interests of all stakeholders**, instead of focusing on the short-term financial interests of shareholders, as part of directors’ duty of care [[15]](#footnote-16)
* 86% of respondents believe sustainability risks, impacts and opportunities should be integrated into a **company’s strategy**, decisions and oversight.[[16]](#footnote-17)
* 60% of respondents believe **stakeholders should be given a role in the enforcement of directors’ duty of care**.[[17]](#footnote-18) It was noted that individual companies and business associations expressed particular concern on this point.

Due diligence duty

* 92% respondents preferred a **horizontal approach** as regards the content of a possible corporate due diligence duty over a sector specific or thematic approach.[[18]](#footnote-19)
* The most preferred option (48.1%) was a **minimum process and definitions approach**, complemented with further requirements.[[19]](#footnote-20) The order of preference differed in the case of individual companies and business associations which preferred a minimum process and definitions approach without further requirements (35.2%).[[20]](#footnote-21)
* Respondents considered that a broad spectrum of **areas** should be covered[[21]](#footnote-22) and that EU level **substantial requirements** should be set using relevant international recognized standards and guidelines[[22]](#footnote-23).
* To **reduce the burden** linked to due diligence for companies, in particular SMEs, respondents indicated that a toolbox/dedicated national helpdesk for companies to translate due diligence criteria into business practices (53%) would be most effective, followed by capacity building support, including funding (42%) and detailed non-binding guidelines catering for the needs of SMEs(34%).
* 97% of respondents agreed[[23]](#footnote-24) that due diligence rules should also apply to **third country companies** which are not established in the EU but carry out (certain) activities in the EU.[[24]](#footnote-25) 91% of respondents also agreed that an EU due diligence duty should be accompanied by **other measures** to ensure a more level playing field between EU and third country companies.
* Regarding an **enforcement mechanism** accompanying a mandatory due diligence duty, 71% of respondents indicated that supervision by competent national authorities with a mechanism of EU cooperation/coordination is the most suited option.[[25]](#footnote-26) [[26]](#footnote-27)
* As regards **access to remedy**, the **main type of difficulties** to get access to remedy as mentioned by respondents are:
  + Too short statute of limitations, especially when the law of a third country is applicable;
  + High costs linked to court procedures;
  + Limited access to evidence for victims and a high burden of proof.
* As to how and in which context these difficulties could be addressed, the following solutions were mentioned most by respondents:
  + Reversal of the burden of proof;
* A reasonable statute of limitation;
* Parent companies in the EU should be liable for harm caused by their subsidiaries or value chain partners located in a third country;
* Victims should be able to rely on EU law, courts should apply the law (whether that of the home state or the host state) that is most favourable to the victim.

Other elements of sustainable corporate governance

* 66% of respondents agreed that directors should establish and apply mechanisms or use existing information and consultation channels for **engaging with stakeholders** in defining corporate strategy and due diligence processes.[[27]](#footnote-28) [[28]](#footnote-29) It is noted that the majority of individual companies and business associations did not agree (68%).
* Regarding options to contribute to countering **remuneration of directors** incentivising short-term focus, the following options were ranked most effective by respondents:[[29]](#footnote-30)
  + Making compulsory the inclusion of sustainability metrics linked, for example, to the company’s sustainability targets or performance in the variable remuneration;
  + Taking into account workforce remuneration and related policies;[[30]](#footnote-31)
  + Requirement to include carbon emission reductions, where applicable, in the lists of sustainability factors affecting directors’ variable remuneration.

Respondents in favour of further regulating remuneration, suggested restricting the use of shares by not allowing them to take effect until several years have lapsed from the date of issue or at least during active employment, or banning the payment of executives with shares or share options altogether. Those disagreeing believe that share-based remuneration is the best way to increase long-term orientation of management and support the goal of sustainable value creation at the company. [[31]](#footnote-32)

A large group of respondents expressed disagreement with the proposed initiative regarding the remuneration of directors. These respondents stated that further EU-regulation is not needed as they believe that the current European hard law framework contains sufficient provisions regarding remuneration structures.

* Regarding **enhancing sustainability expertise** in the boards, respondents ranked the requirements for the board to regularly assess its level of sustainability expertise and take appropriate follow-up (including regular trainings) as the most effective option (56.5%).[[32]](#footnote-33) Individual businesses and business association either did not consider any proposed options effective (42.4%) or shared the preference to regularly assess the level of expertise (39.7%).

Impacts of possible measures

* Respondents believe binding law with targets would have the most **impact** on administrative (mean score of 7.20 on a scale from 0 to 10), litigation (6.48) and other costs (6.83)[[33]](#footnote-34), but would also bring the highest benefits (performance, competitiveness, risk management and resilience, innovation and productivity, environmental and social performance).[[34]](#footnote-35)
* Company/business organisations and business associations give the **costs** of binding law with targets the highest rating (mean is 23.37), followed by NGOs and environmental organisations (mean is 22.70), EU citizens and consumer organisations (mean is 15.57) while trade unions give a low mean rating of 2.00, as presented below.[[35]](#footnote-36)

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | Non-binding guidance | | Binding  law, cost and benefits linked to setting up/improving external impacts’ identification | | Binding  law, annual cost linked to the fulfilment  of possible requirements | |
|  | N | Mean | N | Mean | N | Mean |
| **EU citizens and consumer organisations** | | | | | | |
| Administrative costs | 25 | 2.88 | 26 | 4.73 | 25 | 5.96 |
| Litigation costs | 26 | 3.08 | 27 | 4.19 | 25 | 5.08 |
| Other costs | 23 | 3.13 | 23 | 4.39 | 22 | 5.32 |
| *Total Costs* | *23* | *8.83* | *23* | *12.61* | *21* | *15.57* |
| **Company/business organisations and business associations** | | | | | | |
| Administrative costs | 78 | 2.50 | 86 | 6.17 | 84 | 8.10 |
| Litigation costs | 71 | 1.73 | 80 | 5.88 | 78 | 7.51 |
| Other costs | 73 | 2.07 | 80 | 5.28 | 77 | 7.73 |
| *Total Costs* | *68* | *6.28* | *75* | *17.23* | *73* | *23.37* |
| **NGO’s and environmental organization** | | | | | | |
| Administrative costs | 12 | 2.38 | 11 | 6.27 | 10 | 7.90 |
| Litigation costs | 12 | 1.50 | 11 | 5.45 | 10 | 7.10 |
| Other costs | 12 | 1.75 | 9 | 6.00 | 10 | 7.70 |
| *Total Costs* | *12* | *5.63* | *9* | *18.11* | *10* | *22.70* |
| **Trade unions** | | | | | | |
| Administrative costs | 6 | 0.67 | 6 | 1.17 | 6 | 1.83 |
| Litigation costs | 6 | 1.00 | 5 | 0.60 | 5 | 0.80 |
| Other costs | 6 | 0.67 | 6 | 1.33 | 6 | 2.17 |
| *Total Costs* | *5* | *0.60* | *5* | *1.60* | *5* | *2.00* |

* Trade unions give the **benefits** of binding law with targets the highest rating (mean is 34.43), followed by EU citizens and consumer organisations (mean is 33.73), while company/business organisations and business associations rate these benefits lower (mean is 25.13), as presented below.[[36]](#footnote-37)

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | Non-binding guidance | | Binding  law, cost and benefits linked to setting up/improving external impacts’ identification | | Binding  law, annual cost linked to the fulfilment  of possible requirements | |
|  | N | Mean | N | Mean | N | Mean |
| **EU citizens and consumer organisations** |  |  |  | |  | |
| Better performance | 24 | 4.63 | 26 | 5.42 | 25 | 5.76 |
| Competitiveness advantages | 24 | 5.04 | 26 | 5.88 | 25 | 6.80 |
| Better risk management and resilience | 24 | 5.13 | 26 | 6.35 | 24 | 7.13 |
| Innovation and improved productivity | 23 | 5.09 | 26 | 5.96 | 24 | 6.42 |
| Better environmental and social performance | 23 | 5.78 | 25 | 6.72 | 22 | 7.36 |
| *Total Benefits* | *22* | *26.18* | *25* | *30.20* | *22* | *33.73* |
| **Company/business organisations and business associations** | | | | | | |
| Better performance | 75 | 3.28 | 82 | 4.02 | 80 | 4.60 |
| Competitiveness advantages | 72 | 3.61 | 80 | 4.05 | 78 | 4.24 |
| Better risk management and resilience | 75 | 4.15 | 80 | 5.10 | 80 | 5.80 |
| Innovation and improved productivity | 74 | 3.57 | 79 | 4.03 | 79 | 4.46 |
| Better environmental and social performance | 75 | 4.04 | 81 | 5.21 | 80 | 5.78 |
| *Total Benefits* | *71* | *18.39* | *76* | *22.50* | *76* | *25.13* |
| **NGO’s and environmental organization** | | | | | | |
| Better performance | 12 | 3.83 | 12 | 5.33 | 9 | 5.78 |
| Competitiveness advantages | 12 | 4.00 | 13 | 5.54 | 9 | 6.89 |
| Better risk management and resilience | 14 | 4.57 | 14 | 6.43 | 10 | 7.90 |
| Innovation and improved productivity | 12 | 4.17 | 12 | 4.83 | 9 | 6.89 |
| Better environmental and social performance | 13 | 4.23 | 12 | 7.75 | 10 | 8.20 |
| *Total Benefits* | *11* | *19.55* | *10* | *29.90* | *7* | *34.43* |
| **Trade unions** | | | | | | |
| Better performance | 6 | 1.67 | 6 | 5.33 | 7 | 9.57 |
| Competitiveness advantages | 6 | 1.67 | 6 | 5.50 | 6 | 9.67 |
| Better risk management and resilience | 5 | 1.00 | 6 | 5.50 | 5 | 8.40 |
| Innovation and improved productivity | 5 | 1.00 | 5 | 5.00 | 5 | 9.40 |
| Better environmental and social performance | 6 | 1.67 | 6 | 5.50 | 6 | 9.50 |
| *Total Benefits* | *5* | *5.00* | *5* | *25.00* | *5* | *46.20* |

* The most cited **benefits** of due diligence rules by respondents are:
  + Reductions in harassment, intimidation, threatening and killing of human rights, land and environmental defenders;
  + Safer and more decent working conditions for supply chain workers including health and safety, living wages and decent terms of employment;
  + Reductions in incidents of labour exploitation, worker-paid recruitment fees, debt bondage, human trafficking, other forms of forced labour, and child labour;
  + Reductions in land grabs and violation of customary and other land rights of indigenous people and local communities in host countries;
  + Improvement in the environmental impact of business operations;
  + Creation of long-term and trust relationships through the use of meaningful stakeholder engagement processes and specific risk assessment and response methodologies;
  + Progress towards the achievement of the Sustainable Development Goals.
* Regarding the **costs** of due diligence rules, respondents cited the following:
  + Companies might have to withdraw their business from third countries with weak or absent social, labour, and environmental rules. This could damage global trade and the jobs of employees in developing and emerging countries;
  + Excessive and unnecessary bureaucracy and administrative costs;
  + Legal uncertainty, liability and resource risks, especially for small and medium-sized companies;
  + Increase in prices.

## Results of OPC – campaigns

We identified two campaigns that did not directly use the ”Have your say” portal: (1) Protect People and Planet organised by Anti-slavery International, Avaaz, Clean Clothes Campaign and Global Witness: 450.106 responses, and (2) Friends of Earth Europe and ECCJ, trade unions ETUC, AK Europa and OGB: 22.500 respondents. In this section, we also discuss one response that was submitted through “Have your say”, but that was accompanied by a petition (launched by WeMove and Sumofus) containing 122.785 signatures.

Key points from the Campaigns analysis include:

Need and objectives for EU intervention

* Respondents agreed on the need for a holistic approach that takes account of stakeholder interests in corporate decisions and expressed support for developing an EU legal framework for due diligence.
* While seeing no drawbacks, 22.500 campaign respondents think that a potential benefit of an EU legal framework is better chances to be part of EU supply chains.
* Petition signatories highlighted that the EU should also engage constructively in the negotiations for an ambitious UN Treaty on Business and Human Rights.

Directors’ duty of care – stakeholder interests

* Respondents mostly did not express views about interests relevant for the long-term success and resilience of the company nor the management of risks for the company in relation to stakeholder interests.
* However, some of the 22.500 campaign respondents and petition signatories strongly agreed on the need for action on all elements of directors’ duties, i.e. legal requirement to set up adequate procedures and measurable (science –based) targets; balancing the interests of all stakeholders; sustainability risks, impacts and opportunities being integrated into the company’s strategy; stakeholders (genuine representatives of workers, environment or people) being given a role in the enforcement.

Due diligence duty

* Petition respondents noted that the ‘due diligence duty’ should include a remediation duty, that is, the obligation to actively engage in the remediation of adverse impacts.
* Campaign respondents expressed preference for a minimum process and definitions approach while petition signatories in turn, prefer a minimum process and definitions approach complemented with further requirements.
* Respondents agree on the possibility of the burden for SMEs being reduced with capacity building support or using a toolbox/dedicated national helpdesk.
* Respondents advocated for enforcement, through both supervision by competent national authorities based on complaints about non-compliance with effective sanctions and judicial enforcement with liability.
* Petition signatories believe that the EU directive should apply to all businesses, including multinational enterprises, regardless of their size as well as to certain third-country companies, which is also supported by 22.500 campaign respondents.
* As regards difficulties to get access to remedy, petition signatories and 22.601 campaign respondents highlighted the Boliden[[37]](#footnote-38), KiK case[[38]](#footnote-39) and Shell case[[39]](#footnote-40) as examples for barriers to justice (legal, procedural and practical) in holding European companies liable for the harm caused by their subsidiaries or supply chain partners located in a third country. They suggest that EU laws and rules on jurisdiction should allow for the liability of parent and lead companies, them being required to prove they took all due care. In seeking the right to claim compensation, victims should be able to rely on EU law, which should provide for reasonable time limitations for bringing legal actions.

Other elements of sustainable corporate governance

* Respondents agreed that the EU should require directors to establish and apply mechanisms for engaging with stakeholders in this area.
* The campaign respondents believe advisory bodies should be promoted at EU level, but stakeholder general meeting and complaint mechanism as part of due diligence should be best practice.
* Neither the campaign respondents, nor the petition respondents ranked the provided options concerning remuneration of directors in terms of their effectiveness
* 22.500 campaign respondents and petition signatories believe enhancing sustainability expertise in the boards is necessary through all listed options[[40]](#footnote-41) and support EU taking further action to regulate share buyback.

Impacts of possible measures

* Respondents did not rate any of the costs or the benefits.
* Campaign respondents highlighted expected positive impacts of mandatory duty of care and due diligence duty on stakeholders and the environment through; reductions in harassment, killings of human rights, land and environmental defenders; safer working conditions and decent terms of employment for supply chain workers; reductions in incidents of labour exploitation, human trafficking, worker-paid recruitment fees, debt bondage, forced labour and child labour; help in addressing root causes of poverty, discrimination and lack of education; reductions in land grabs and violation of the rights of local communities in host countries, including indigenous peoples and forest communities; reduction of deforestation, use of pollutants and emission of greenhouse gases.

## Results of position papers

Besides the online questionnaire, stakeholders could also present their view on the initiative by means of a position paper. In total 149 position papers were reviewed, of which 65 papers were left out of the review for various reasons (e.g. most consisted of a copy of the online survey submitted through “Have your say”). As regards Member States, three submitted a position paper: Denmark, Sweden and the Netherlands.

Multiple respondents indicated that they found the online questionnaire to be biased and difficult to answer. A handful of these respondents did not fill in the questionnaire for these reasons and instead present their view on the initiative via a position paper.

Key points from the position paper analysis include:

Directors’ duty of care – stakeholder interests

* Similar to the feedback to the inception impact assessment (roadmap), various position papers were critical of the Supporting study on directors’ duties, the methodology applied and its assumed sole usage as the basis for the initiative. These assumptions could be one of the reasons why they did not support EU legislation on this matter.
* It was noted that the public consultation does not take sufficient notice of the feedback that the study has received from multiple academics[[41]](#footnote-42), business organisations, institutional investors and self-regulation bodies.

Due diligence duty

* Respondents from EU Member States that submitted a position paper (Denmark, the Netherlands, Sweden) are in favour of a coordinated horizontal European approach on due diligence built upon the already existing international standards. Sweden stressed that the legal framework should cover third-country companies, cover all business, and have a system for follow-up.
* Regarding the scope, most respondents regardless of their category highlighted the objective of levelling the playing filed by covering all companies, regardless of size, sector or type of incorporation, including non-EU companies with operations in the EU.
* There was agreement on the need to take account of the needs and specificities of SMEs with the scope of obligations and accountability being differentiated by the risk profile of companies.
* As regards liability, respondents were not in favour of civil liability in the event of a breach of the duty of care and in the event damages could not have been foreseen or prevented under the due diligence obligation. However, they suggested companies should be liable for damages caused by their business relations with which they have a direct connection.

Other elements of sustainable corporate governance

* The view on remuneration is mixed with respondents either favouring remuneration being linked to the achievement of the targets sets in the strategy or seeing no need to link remuneration with the strategy, as companies are best placed to align remuneration with their long-term corporate goals.
* Respondents were of the opinion that companies should consider sustainability expertise in the directors’ nomination and selection process.
* A handful of respondents stated that there should not be a legal requirement to have a certain number of board members with sustainability expertise.
* Multiple respondents indicated that there should be a specific board member that is responsible for the design and implementation of a company’s ESG strategy.

Impacts of possible measures

* The most commonly cited potential negative impacts and benefits of EU regulation by respondents in the position papers are in line with the OPC results presented above.

Separation of due diligence and directors’ duties

* Several respondents, including the Swedish and Danish government believe that the two sections of the EU initiative (i.e. due diligence and corporate governance/directors’ duty of care) should be split and treated independently from one another.

# Social partners dialogue

A dedicated hearing on the sustainable corporate governance initiative took place on 22 February 2021 by videoconference. The background paper was shared with all 87 EU social partners while not all could participate in the hearing.The participants included the employers’ delegation, consisting of 20 organisations[[42]](#footnote-43) and the trade union delegation, consisted of 19 organisations[[43]](#footnote-44), including European and MS associations from Denmark, Finland, Bulgaria, Czechia, France, Germany, Austria, Netherlands, Sweden, Germany, Italy and Spain. This consultation aimed at collecting social partner’s views and experience on the possible sustainable corporate governance measures, in particular on the need for EU level intervention, essential features of the initiative necessary to deliver on its objectives, experience of measures that have/have not worked well, enforcement mechanism of the planned duties and possible need for additional measures.

All social partners were invited to send written contributions. 7 organisations submitted written input in reaction to the background paper presented by the Commission.

Key points from the social partners’ dialogue include:

Directors’ duty of care – stakeholder interests

* Employers’ organisations voiced concern about the need for legislative intervention as it might put into question the fundamentals of freedom of enterprise and property/ownership. Obstacles identified were mostly linked to diverging interests of stakeholders.
* The need to preserve the flexibility of employers was stressed in order to determine not only the relevance of specific stakeholder groups to their activity and how they interact with them, but also to assess whether different interests are material to the company over the short, medium and long-term. Therefore, flexible solutions were advocated, e.g. allowing companies to define their own strategy, in accordance with their activities and geographical context, giving due regard to stakeholders’ interests.
* In contrast, trade unions considered that clear and broad definition of directors’ duties and the company’s interest should be defined in EU law, including requirements for corporate boards to integrate sustainability aspects (risks, opportunities, impacts) into the business strategy and to set sustainability targets aligned with international agreements and guidelines.
* Trade unions were of the opinion that these measures can substantially contribute to a reorientation of directors’ interests away from the short-term towards long-term sustainability interests, drive better long-term performance and resilience as well as corporate investment into human capital development and better working conditions.
* In addition, in order to ensure that directors promote sustainability, trade unions suggested the mechanism of an EU-wide definition of ‘disqualified director’, including disrespect for human rights and the environment as grounds for disqualifying persons from duty as directors.

Due diligence duty

* Employers’ organisations saw the benefit of mandatory rules based on UNGP and OECD standards in avoiding a patchwork of national rules that drive up costs.
* Employers’ organisations advocated for a reasonable burden for companies cautioning about the impact on international trade, competitiveness and possible divestment from and avoidance of complex markets.
* They highlighted the importance of restricting legal obligations to what companies can reasonably be expected to control without deterring them from going beyond their legal obligations (e.g. first tier); taking account of the needs of SMEs; striving towards the spread of standards globally by exerting leverage internationally.
* Caution was advised on referencing the global systemic issue climate change (GHG emissions), considering it is best addressed by other means than due diligence.
* Some questions were raised about the need for further substantiating the legislative intervention at EU level, considering that the current mechanisms in place might suffice in driving responsible action and calling for the EU to undertake an effort to push forward common approaches at international level
* Furthermore, questions on clarifications on the methodology applied to estimate costs to comply with due diligence were raised which has been addressed in detail in the assessment of impacts.
* Trade Unions expressed support for EU level action on a mandatory and effective due diligence framework covering companies’ activities and their business relationships.
* They saw benefit in the personal scope covering all companies established or active in the European Union, regardless of their legal form.
* They stressed the importance of a gender-sensitive approach emphasizing the rights to collective bargaining and freedom of association, requiring due diligence to identify and mitigate risks to these rights, and remediate in cases they are violated, the necessity of meaningful trade union engagement as well as integration of sustainability aspects into the core business strategy.

Enforcement

* Employers’ organisations considered it could be left to MS to determine, in accordance with their existing legal frameworks, which measures or penalties for infringement of the due diligence obligation are required.
* It was stressed that companies should be able to demonstrate that they have put in place appropriate due diligence measures and that where a human rights impact has occurred despite such appropriate measures, there are provisions for access to remedy which can be facilitated through accessible and effective operational-level grievance procedures clearly defined in the law.
* Employers’ organisations highlighted that companies should be required to report on the due diligence process to a Competent Authority which powers should be limited to verification.
* Trade Unions, as employer’s organisations, agreed that liability should be linked to cases where companies fail to respect their due diligence obligation of means.
* Similarly, trade unions also agreed with employer organisations on the need for effective remedies. However, they specifically stressed that the directive shall not impact on other subcontracting and supply chain liability frameworks established at national, European and international level (e.g. joint and several liability in subcontracting chains).

Separation of due diligence and directors’ duties

* As in the case of OPC position papers, some trade unions and employer organisations suggest considering separating the proposal on the directors’ duties from corporate due diligence.

# Targeted consultations

A number of targeted consultation methods were performed since the announcement of the Roadmap, including more focused interactions and dialogues in stakeholder workshops and meetings, where more specific expertise was sought.

## Meetings with Member State representatives in the Company law Expert Group (CLEG)

Two meetings with Member State representatives in the Company law Expert Group (CLEG) took place as part of consultation activities.

The objective of the first CLEG meeting on sustainable corporate governance, which took place virtually on 16 December 2020 was to receive first comments from Member States on their approach to the topic including an update on national initiatives. First feedback showed that while the due diligence element found overall general support, some interventions on directors' duties were more hesitant (mainly DK, SE, EE).

The objective of the second CLEG meeting on sustainable corporate governance, which took place on 28 April 2021, was to present the results of the open public consultation, and obtain feedback from Member States. Overall, mandatory EU due diligence legislation found general support from intervening Member States[[44]](#footnote-45), with views on scope varying[[45]](#footnote-46). Interventions on directors’ duties were more hesitant and critical, with certain Member States[[46]](#footnote-47) questioning the need for action in this sphere.

## Meeting of the informal company law expert group mainly composed of company law legal academics (ICLEG)

The ICLEG meeting of the subgroup on sustainable corporate governance, which took place virtually on 8 February 2021, focussed discussion on the key objectives of the initiative. On the topic of personal scope of the obligation, several members noted that while the objective should be to cover all companies, the possibility of a gradual approach with a narrower scope could also be considered. Other elements highlighted in the meeting were related to the possibility of envisaging proper compliance of due diligence processes and requirements as a defence from liability in case of harms caused in the value chain. Several members were of the view that a clear legal obligation would provide legal certainty for companies; legal certainty being indispensable for the business environment. One member mentioned mediation and other alternative dispute resolution mechanisms as an important and useful tool to solve conflicts under this framework.

## Conferences and stakeholder meetings

In the consultative and analytical phase leading up to the announcement of the initiative in the CWP 2021 and publication of the inception impact assessment (roadmap), as well as thereafter, a number of conferences and meetings with business associations, individual businesses, including SMEs representatives, civil society, including non-governmental and not-for-profit organisations as well as OECD took place. At technical level, approx. 70 such exchanges took place only since the publication of the roadmap, out of which approx. half were multi-stakeholder conferences, which provided for a useful platform to gather views on specific issues from a number of stakeholders. Particular attention was paid to ensuring stakeholder balance in the process, including geographical. These fora as well as a number of those that took place at political level, provided an opportunity for stakeholders to provide their input and voice any concerns. The follow-up to these exchanges consisted in reflection on the elements in the larger context and use of relevant input in the assessment of impacts of policy options.

1. Who is affected and how?

# Practical implications of the initiative

The initiative will have practical implications for companies falling under the scope (including their directors), for companies that are in the supply and value chains of such companies, for third countries and their companies, as well as for public authorities involved in the enforcement.

Companies and their directors will need to establish or adjust the organisational functions, set up the necessary systems, procedures and processes in order to comply with the due diligence and risk management obligations. Furthermore, where necessary for impact mitigation or risk management purposes, companies will need to change their business practices and production processes, reorganise their supply and value chains, and possibly even change their business models. A company with a business model which is more closely linked with possible adverse human rights or environmental impacts is likely to need to do more in this regard.[[47]](#footnote-48)

The necessary changes will often require investments into the workforce, increased capital expenditure or more long-term R&D projects, more consultations and engagement with employees, customers, environmental organisations, local communities, as well as with other enterprises in the value chains. More cooperation with other companies in the sector or in the same value chain is expected not only where this is specifically required but also because this can improve efficiency. As a result of possible changes relating to directors’ remuneration, some minor compliance and adjustment costs are also expected for companies.

The task of supervision will have to be allocated to existing authorities or to a newly set up national authority. Cooperation forms with other competent authorities, in the same Member State and possibly in others, will need to be established. Expertise and capacity to receive and investigate complaints has to be built. Also, supporting measures will need to be developed (at EU and Member State level) for companies to ensure proper implementation as well as in producer countries.

# Summary of costs and benefits

The following table summarizes the benefits of the combination of the preferred options for the various stakeholder groups impacted by the initiative. While there is growing evidence on benefits for the companies that would be regulated by the initiative, which are often quantified and monetized, we will only explain these expected benefits in qualitative manner in this summary. It is to be stressed at the outset that not all companies will benefit from the new measures to the same extent: for instance, companies operating in sectors where the transition risks are high will benefit more from proper risk management, while companies which have built their business models on sourcing from low-standard countries may lose their competitive advantage in global markets. For specific details on the findings of relevant research please refer to Annex 4 as well as the main body of this report.

Benefits for other stakeholders, including in particular the expected positive human rights and environmental impacts, cannot be expressed in monetary terms. As the initiative aims at making the highest possible positive contribution in these areas in the given context, an absolute quantification of the benefits for other stakeholders was deemed not necessary nor possible.

| ***I. Overview of Benefits (total for all provisions) – Preferred Option*** | | |
| --- | --- | --- |
| ***Type*** | ***Description/ who will benefit*** | ***Comments*** |
| ***Direct benefits*** | | |
| Companies **improve the management of their financial and non-financial risks**, including those resulting from climate change and environmental degradation, or from human rights, labour and social factors and which may arise from their value chain.  Companies **build production processes with reduced adverse external impacts** | Better risk identification and risk management improves the company’s **resilience,** allows the company to identify dependencies, **respond to changes**, including raw material shortages, or to crisis situations, avoid losses. Holistic risk management improves long-term value creation and **longer-term profitability.**  Building production processes more respectful of human rights and the environment may result in **cost reductions, operational efficiency**, **innovation**, may result in competitive advantages. For example **low carbon investments typically yield cost savings in excess of the initial investment at an average profit of EUR 17 per tonne of CO2**. They may also lead to **new revenue opportunities**. Climate investments pay back in relatively short time.  Who will benefit?  **The company - large and small - including its members, shareholders** **other stakeholders**, such as **employees** (interested in the viability and performance of the company, benefit from investment into human capital, etc.) **the environment**, **affected people, creditors**, etc. | Other related benefits for the company include:  -better knowledge of value chain, production processes,  -better commercial relationships,  -more trust from stakeholders, customers  -better access to capital, etc. |
| **First mover advantages in global markets**, better mid to long-term competitiveness in global markets | As the transition offers opportunities, first movers may gain competitive advantages on global markets due to growing demand for sustainable products.  As additional company level costs per revenue is relatively low, no significant negative distortions for EU exporter are expected. At the same time, EU companies could get first mover advantages including securing access to resources, technology, secure market shares in global markets and gain economies of scale vis-a-vis later market entrants.    This will benefit the **company**, its **shareholders, investors, creditors**, **employees and other stakeholders**. |  |
| Companies **reduce their adverse human rights, health and social impacts** | While right-holders will have improved access to justice, the due diligence requirement will also bring preventative benefits for the right-holders. Victims or possible victims of adverse human rights impacts in the EU and in third countries will be directly impacted.  Who will benefit?  **the company, its employees, those of value chain partners, local communities, third countries, etc.** |  |
| Companies **reduce their adverse impact on climate, biodiversity, pollution,** etc. | Both preventative benefits, stopping harmful activities and impact mitigation is expected.  Who will benefit?  **All the society, the environment, the economy, third countries, companies and their stakeholders** |  |
| ***Indirect benefits*** | | |
| **Resilience, and mid-to long-term competitiveness benefits for the EU economy** | The cumulative medium to long-term net benefits for corporations are expected to result in medium to long-term competitiveness gains for the economy. Better risks management, lower dependency on increasingly scarce natural resources, better resilience to sustainability related shocks and impact mitigation will contribute.  Who will benefit?  **EU economy and indirectly impacted third countries** |  |
| **Sustainable and fair economy and society** | Reduction of climate and environmental footprint, improved human rights, health and other social impact on workers and people will contribute to better conditions for life including in third countries for **current and future generations.** |  |

The following table summarizes the total costs of the preferred options, including quantifiable compliance costs for companies (these are the theoretical maximum aggregate business compliance costs) and the enforcement costs for the public authorities designated by Member States for supervision.

| ***II. Overview of costs – Preferred option*** | | | | | |
| --- | --- | --- | --- | --- | --- |
|  | | **Compliance costs for businesses**  (in EUR) | | **Supervisory costs for national authorities**  (in EUR) | |
| **One-off** | **Recurrent** | **One-off** | **Recurrent** |
| **Corporate due diligence obligation (option 3a/3b), directors’ duties option 3, and remuneration measures** | **Direct costs** | 1.13 billion /  0.94 billion  + Cost of transition to sustainability (not quantified, but qualitative and quantitative examples with cost ranges are given)  + Costs related to adjustment of existing remuneration policies and reporting have not been quantified but should remain minimal. | 2.37 billion /  1.72 billion  No other additional recurrent cost is expected. | 0.13 million | 11.24 million / 7.86 million |
| **Indirect costs** | Indirect costs will be implied by the due diligence obligation and they are only partly quantified and included in the numbers on direct costs. Compliance costs could **trickle down** to companies (including SMEs) which are not under the scope but belong to the value chain or group of a (large) company covered by the regulation.  We have calculated with the cost of targeted due diligence for those value chain companies which operate in high impact sectors and which would be indirectly impacted through the obligation of the very large company. | | N/A | N/A |

1. *Estimates are provided with respect to the baseline,;*
2. *Aggregated direct costs for companies are likely to be overestimated because of the cautious calculation method of calculating firm-level costs and because certain sectors regarded as high-impact may be further refined, thus reducing the number of companies under the scope;*
3. *One-off costs for companies are not immediate costs and can be spread across several years.*
4. Identification and assessment of impacts

# Introduction

This annex shows the findings of the identification (“screening”) and assessment of potential significant impacts of addressing the market and regulatory failures identified in the problem definition by the measures included in the policy options retained for a detailed assessment. For this assessment we used the Commission’s [Better Regulation Guidelines](https://ec.europa.eu/info/sites/info/files/better-regulation-guidelines.pdf)[[48]](#footnote-49), and in particular [Tool #19](https://ec.europa.eu/info/sites/info/files/file_import/better-regulation-toolbox-19_en_0.pdf) and [Tool #58](https://ec.europa.eu/info/sites/default/files/file_import/better-regulation-toolbox-58_en_0.pdf) from the related [“Toolbox”](https://ec.europa.eu/info/sites/info/files/better-regulation-toolbox_2.pdf), and matched the impacts with the drivers and consequences outlined in the problem definition section.

The analysis in this annex is based mostly on detailed input from desk research and stakeholder consultations conducted over a prolonged period of time. During the analysis some data gaps were identified. Therefore different studies and research analysing similar information were compared, and assumptions based on expert judgement used in those studies were relied on to ensure the robustness of the analysis.

The assessment is done in a qualitative way, complemented whenever possible by a quantitative assessment which relies on some estimates from the extensive literature review and consultations.

# Screening of economic, social and environmental impacts

In line with the Better Regulation Guidelines, we first screened the possible impacts and established a long list of those which could potentially arise under one or more of the policy options assessed in detail. The starting point for the development of the list of impacts was the typology of impacts in tool #58 and the checklist of impacts in tool #19. The following **potentially significant impacts** were put on this long list:

| Impact type | Long list of impacts |
| --- | --- |
| **Economic Impacts** | * Macro-economic environment (growth, investment and resilience) * International trade and investment flows * International competitiveness * Functioning of the internal market and competition * Innovation, research and technological development * Benefits in terms of business performance * Direct and indirect business compliance costs and litigation costs for businesses * Impact on firm-level cost competitiveness * Impact on SMEs * Impact on economic operators in third countries * Enforcement costs for public authorities * Consumer prices and choices |
| **Social Impacts** | * Employment * Working conditions, incl. wages, employee satisfaction, training and health, also in third countries * Social protection of vulnerable groups and local communities, including in developing countries * Inequality, distribution of wealth * Fundamental rights and human rights, including in third countries * Health of consumers |
| **Environmental impacts** | * Fighting climate change * Sustainable production, incl. efficient use of resources and circular economy * Biodiversity, ecosystems, fighting pollution, and minimizing environmental risks, including in third countries |

The screening took into account:

Direct and indirect impacts, including indirect effects encountered by companies that do not fall under the scope of the measure but that will be affected as belonging to the value chain of a directly impacted company;

Positive and negative impacts, including e.g. the benefits to the environment, human rights and businesses, and the costs for businesses;

One-off and recurrent impacts, including e.g. one-off cost of setting up IT systems and the recurrent cost of gathering information on suppliers;

Short and long-term impacts, including e.g. initial gathering information, on-going monitoring of value chain and long-term costs of restructuring production processes.

Based on the above screening, **we prioritised the potentially significant impacts for more detailed analysis**. These are listed in the following table, **clustered** into larger impact categories. This table also identifies the **stakeholder groups affected** by each of the selected impacts, as well as the **general approach that will be used to assess** the impacts, i.e. to what extent they will be approached quantitatively or qualitatively. For the qualitative assessment, we rely on a combination of opinions of stakeholders (given during the interviews conducted for the supporting studies, the input from the open public consultation and other stakeholder consultations), the supporting studies more broadly and other literature we screened, including studies published only recently. For the quantitative assessment, the source of the data is indicated in the assessment.

*Selected potentially significant impacts for each of the stakeholders and the method of assessment:*

| **Impacts** | **Affected stakeholders** | | | | | | | **Assessment** | |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| Economy | Society, citizens, consumers | Workers, incl. in supply chains | Businesses | Public administrations | Third countries | Climate and the environment | Qualitative | Quantitative |
| 1. **Economic impacts** | | | | | | | | | |
| Benefits for business performance | ● |  | ● | ● |  | ○ |  | ● | ○ |
| Business compliance costs |  |  |  | ● |  | ○ |  | ● | ● |
| Litigation costs for businesses |  |  |  | ● |  | ○ |  | ● |  |
| Firm-level competitiveness |  |  |  | ● |  | ○ |  | ● | ○ |
| Enforcement costs for public authorities |  |  |  |  | ● |  |  | ● | ● |
| Resilience of the economy | ● | ● | ● | ● | ● | ● |  | ● |  |
| **B. Social impacts** | | | | | | | | | |
| Working conditions, incl. wages, employee satisfaction, training and health, also in third countries | ● |  | ● | ● |  | ● |  | ● | ○ |
| Social protection of vulnerable groups and local communities |  |  | ● |  |  | ● |  | ● | ○ |
| Fundamental rights/human rights |  | ● | ● |  |  | ● |  | ● | ○ |
| **C. Environmental impacts** | | | | | | | | | |
| Sustainable production, minimizing environmental risks, incl. with regard to climate change, biodiversity loss, degradation of ecosystems, and pollution (incl. in third countries), efficient use of resources and circular economy | ● | ● |  | ● |  | ● | ● | ● | ○ |

For businesses the distinction between **various types of businesses** can be made. Among many different factors explained in the subsequent sections, the impacts for companies differ based on their **size**, on their **activities or sectors** (e.g. high-impact versus low-impact sectors), their place in the value chain, but also on the previous efforts of the company regarding sustainable corporate governance, including if it is already conducting due diligence partially or even across the whole value chain and the whole spectrum human rights and environmental aspects. A significant portion of large EU companies already carry out some form of due diligence, even if limited, and they will face less costs than companies that have yet to start paying attention to due diligence. Similarly, companies will also face lower compliance costs if they are already reporting on sustainability-related matters, and costs attributable to this initiative will also be relatively lower for companies that will be subject to the new sustainability reporting rules (under the CSRD) or which are already subject to sector specific due diligence requirements. We will come back to these differences in the literature review and in the subsequent detailed quantitative assessment of the costs.

# Assessment of possible impacts based on screening of literature and stakeholder consultations

As a second step, we screened the available literature, including the two Supporting Studies, and assessed the results of our stakeholder consultations, with a view to understanding the likely significance and magnitude of each possible impact on the various stakeholder groups, and the strength of their link to this initiative.[[49]](#footnote-50) Our findings will be summarized in a table after the literature screening.

It is worthwhile to note at the outset that many of the screened impacts are **inter-related and inter-dependent**. As it will be shown later in this section, this is equally true for impact types within a certain impact category (e.g. for firm-level benefits or costs[[50]](#footnote-51)) and also for the impacts across the categories (in particular as regards the impact on individual companies which can add up to have an impact on the economy as a whole, or as regards the overlap between certain human rights and environmental matters). The screening process will therefore attempt to identify these various elements but, where relevant, we will **cluster** them at the end of the screening process into coherent impact categories which, in the next phase, can be considered for further analysis.

The impacts vary for different policy options in terms of their extent and significance. However, most impacts are relevant in all policy options. The screening analysis is therefore undertaken **for the options collectively** rather than individually, with a view to assessing the differences in impacts between the options in more detail in the impact assessment.

In the same vein, the impact of the various regulated matters (due diligence, directors’ duties and directors’ remuneration) are closely interrelated, reflecting the fact that corporate and directors’ duties, as well as incentive (remuneration) structures complement and reinforce one another. Therefore, in this annex we will first **consider the impacts of the possible options in all these areas together**, and the detailed assessment of the individual options for each of the three areas will then identify the impacts which are expected to be the most relevant in the options concerned.

## Possible benefits for companies

### Literature review on benefits for companies

The possible benefits of this initiative on companies are manifold. For assessing them, we will rely on the **supporting studies,** **including the supporting study on due diligence,** which includes a thorough review of relevant literature on the possible impacts of mandatory corporate due diligence[[51]](#footnote-52) and a stakeholder survey, as well as on the **literature review of the OECD** on the benefits of due diligence and sustainable business practices.[[52]](#footnote-53) In addition, we took into account **other research and studies, including hose referred to in the problem analysis and divers sections**.

Research in this field focuses on the **economic benefits for companies linked to their improved sustainability (ESG) performance and to their sustainable corporate governance practices in a broad sense** (including due diligence, stakeholder-oriented governance, sustainability reporting, CSR activities, etc.). We will first give an overview about how the financial performance of companies can be affected by switching to sustainable *modus operandi*. Then, we will assess more closely the various areas where benefits can arise, possibly in the form of revenue increases or cost reductions, affecting the bottom line in the short, medium or longer time horizon.

While literature discusses the possible benefits for businesses, it also shows the possible downsides of imposing mandatory requirements to address sustainability risks and impacts: for a certain portion of companies the benefits will be lower, or costs may outweigh benefits, in particular in the short run. For example, for companies which source from countries with low human rights and environmental standards and which face high transition costs for restructuring their value chains, the initial cost impact may be considerable compared to possible benefits, at least in the short run. Furthermore, companies operating in markets with high transition risks will face bigger costs and possibly less benefits in the short term.

**Overall corporate financial performance**

The search for a relation between environmental, social and corporate governance (ESG) criteria and corporate financial performance (CFP) can be traced back to the beginning of the 1970s. In 2015, a seminal meta-analysis of about 200 different sources (ranging from academic articles, industry reports to even books) from between 2005 and 2015 found a **remarkable positive correlation between diligent sustainability business practices and economic performance**.[[53]](#footnote-54) Another, larger meta-study of the same year analysed more than 2000 empirical studies published by scholars and investors on this relation.[[54]](#footnote-55) The results showed that **the business case for integrating ESG factors into corporate decisions is well founded**: roughly 90% of the analysed studies found a non-negative ESG-CFP relation, and the large majority of studies reported positive findings, while the **positive ESG impact on corporate financial performance** appeared to remain **stable** over time.

Furthermore, a very recent meta-study, looking at more than 1000 studies published between 2015 and 2020[[55]](#footnote-56), supports the earlier conclusions: more than 90% of the studies found a non-negative ESG–CFP relation and, more importantly, close to 60% of the studies reported positive findings. Only 8% of the assessed studies found a negative relationship between ESG and CFP. The share of studies showing non-negative relationship was even higher (94%) among the studies focusing on climate change (low-carbon studies)[[56]](#footnote-57). The study also showed that the positive impact of ESG on CFP becomes **more marked over longer time horizons**[[57]](#footnote-58). Other studies have also shown that **failing to pay enough attention to sustainability factors poses** **significant risks to the company** as it can negatively affect its financial performance. For example, an analysis of corporate fines and settlements demonstrates the financial impact of neglecting sustainability issues[[58]](#footnote-59).

**Good reputation**

In the survey conducted for the Supporting study on due diligence (p. 453), multiple companies indicated that reputational risks are or have been their primary incentive to undertake due diligence. Improved reputation brings benefits to the company via several channels, including in the product and services market and the labour market. These are explained under separate points below (a, b).

In general, companies would benefit from improved reputation especially vis-à-vis other companies which are not following the same standards. If a large part of European companies are obligated to conduct due diligence measures to a similar extent, one could benefit substantially less in terms of reputational improvements. However, European companies could still benefit from reputational effects in global markets vis-à-vis non-European competitors and from the potential first movers’ advantage in the global market (Study on due diligence, p. 462).

At the same time, it is likely that the most significant reputational benefits from mandatory due diligence will result from the reduction in existing reputational risks rather than from an enhancement of existing reputational benefits (Study on due diligence, p. 453). A 2009 meta-analysis of 251 studies[[59]](#footnote-60) revealed that a misconduct by the company, if revealed, has a more pronounced effect on its financial performance than if the company would be trying to do good.

Improved brand value, customer loyalty and related financial benefits

The environmental and social commitment of a company can enhance its reputation which, in turn, can improve brand value and customer loyalty. Among customers, there has been a growing desire for products that have been produced in an ethical and environmentally sustainable way without using harmful substances. The growing demand makes it possible to charge price premiums and increase profit margins, which helps the company gain a competitive advantage (OECD study, Table p. 8 and Annex G, p. 60). A large poll of 30 000 consumers revealed that about 1 in 2 of them checks the product packaging to ensure the product has a sustainable impact (OECD Annex C, p. 39). Another study found that consumers perceived greater benefit and value from products sold by a socially responsible company. Consumers were willing to pay 10% more for such products.

However, the extent to which sales increase depends on a great number of firm- and sector-level characteristics and it was pointed out that reputational effects mainly work for companies which are consumer-focused and they are less of a benefit for intermediaries or companies who work in public procurement or in the public sector[[60]](#footnote-61). Also, smaller companies are less likely to financially benefit from reputation-induced benefits: due to their small size, a reputation-based increase in total sales is less likely to generate additional income that is sufficient to cover the additional costs resulting from new due diligence requirements[[61]](#footnote-62).

Attracting, retaining, motivating highly-skilled employees and related financial benefits

Good reputation relating to working environment can help a company obtain competitive advantage (OECD, Table “Summary of Benefits of RBC in General, p. 8) by attracting better performing staff members. Good reputation with respect to corporate working environments can translate into superior stock performance. A study[[62]](#footnote-63) from 2011 found that a portfolio of the ‘100 Best Companies to Work For’ earned an annual alpha of 3.5% in excess of the risk-free rate from 1984 to 2009 and 2.1% above industry benchmarks. Similar outperformance has also been observed for a more extended period from 1984 to 2011. Furthermore, job satisfaction can improve firm value through worker motivation”.[[63]](#footnote-64) Millennials and Gen Z, who are climbing the corporate ladder now, have more pronounced preferences for sustainability. Firms in more environmentally friendly sectors are not only better able to attract and retain workers that are highly skilled but they can do that at lower wages.[[64]](#footnote-65)

The report evaluating the application of the French due diligence law[[65]](#footnote-66) finds that improving working conditions and sustainable operations motivate workers and help attracting the most qualified people who look for jobs which have a meaning and respect of values. This increases the competitiveness of French businesses subject to the law vis-à-vis companies that are not under its scope.

However, as explained above, **these benefits are less pronounced when obligations apply to a large number of companies**, but they remain relevant for companies operating beyond EU markets.

* **Lower cost of capital, better access to capital**

A recent meta-analysis of 200 studies revealed that in about 90% of the studies evidence was found that companies with solid sustainability practices face lower capital costs (OECD Annex G, p. 60).[[66]](#footnote-67) Cost of capital is directly linked to a company’s risk level and profitability.

Financial institutions are more likely to demand evidence of sound sustainability standards. The increased transparency and **reduced business risks** **can lead to lower borrowing costs** (i.e. lower cost of capital) and it opens the companies’ access to financing sources they would otherwise not have had access to (OECD Annex G, p. 60). The due diligence study supports these claims and found a positive relationship between the corporate social performance of the company and its debt rating (Study on due diligence, Annexure IV Table 9).

Companies with good sustainability practices may also appear more attractive to other investors due to the expectation of lower risks and reduced information asymmetries from disclosure standards[[67]](#footnote-68).

Another study revealed that the cost of equity can be reduced by 1 % as a result of good environmental, social and governance (ESG) practices[[68]](#footnote-69), although one study points out that this negative relationship between environmental performance and the cost of capital differs across geographies, time periods, choice of method and choice of sustainability measures (Study on due diligence, Annexure IV Table 9 p. 75).

* **Improved market value of the firm**

Not only the financial performance of a company can be influenced by the companies’ ESG policy but also its stock price may be impacted positively or negatively (Study on due diligence, p. 452; OECD, Annex C p. 41). Multiple studies confirmed this as they found that:

- good RBC and sustainability efforts are rewarded by superior stock performance (OECD Annex G, p. 60);

- negative ESG events lead to 0.65% to 0.76% drop in stock prices on the day the event occurs (OECD table p. 10).

Another study found less volatility in the stock performance of companies that incorporated ESG factors into their policy compared to those who did not (Study on due diligence, Annexure IV Table 12 p. 80);

Results of a comparison of stock price performance related to the companies’ sustainability policy show that high sustainability companies outperform low sustainability ones annually with about 5%. Important to note is that the results also suggest that this outperformance only occurs in the long term (OECD Annex C, p. 35). Another study also suggests that the benefits of CSR are not immediately valued by the market (OECD Annex C, p. 44).

**Better stock performance was also demonstrated in crisis situations, such as the Covid** crisis. A study conducted during the first wave of the crisis[[69]](#footnote-70) suggests that firms which responded to the pandemic with a credible commitment to their stakeholders and incorporated their impacts on employees, suppliers, and customers in their decisions demonstrated stronger relative stock price performance after the outbreak of the pandemic. Furthermore, the OECD note referred to above[[70]](#footnote-71) projected that companies paying attention to their impacts on workers and supply chains have better prospects for recovery in the medium to long term. A study published by the European Capital Markets Institute finds that “companies integrating an ESG approach recognised by investors and ESG funds have been more resilient in the crisis”, and goes on to conclude that “investors’ taste for ESG has not lessened during this crisis – quite the opposite, in fact.”[[71]](#footnote-72)

* **Better risk management and resilience**

Better management of stakeholder related risks can significantly improve the company’s performance and strengthen its resilience. This benefit is unlikely to reduce due to the compliance of many other EU companies with the same duty.

According to the 2019 World Economic Forum Report on Global Risks[[72]](#footnote-73), **today’s most urgent business risks are directly linked to sustainability issues**: e.g. failure of climate-change mitigation and adaptation, extreme weather events and natural disasters. Such evolution in the risk landscape means that sustainability risks “that were once considered “black swans” are now far common – and can manifest more quickly and significantly”[[73]](#footnote-74). As explained above, environmental risks, if materializing, can have significant financial impact on the company. For example, the impact assessment of the EU Climate Adaptation strategy states that with record high temperatures in 2020 globally and across much of Europe, and with a clear message from climate models that temperatures will continue to increase, the urgency to adapt seems undeniable. The IPCC Special report shows that even in a best-case scenario of sustained emission limitations, and global warming limited to 1.5°C, there will be severe stress on agri-food systems, infrastructure, ecosystems, natural capital, etc. An academic study assessing the impact of corporate social performance on market-based company risk in Europe[[74]](#footnote-75) found that better corporate social performance – especially in the social dimension – can increase company value through lower company risk.

Furthermore, management of risks related to **value chain issues (adverse impacts, raw material shortages, etc.) contributes to avoiding losses and ensuring sustained performance. Deeper knowledge of operating processes** helps avoid the impact of a negative event on its reputation and financial performance which otherwise take a company several years to recover (OECD Annex G, p. 59).

McKinsey interviewed leaders from sustainable companies in 2014[[75]](#footnote-76), showing that effective risk management can have a substantial economic impact for a company. The economic value at risk as a result of reputational risks (e.g. reputational damage based on perceived misuse of resources) is estimated at 70% of a company’s earnings, the value at stake from risks related to rising operation costs (e.g. increasing raw-material costs due to increased demand/lower supply) is estimated at 60%, and the value at stake from risks related to possible supply chain disruptions is 25% (e.g. production delay or cancellation due to lack of access). The recent meta-study referred to above also pointed out the role of improved risk management and more innovation driven by the company’s ESG initiatives in improved financial performance).[[76]](#footnote-77)

Some of the stakeholder-related risks and the need to address them properly have gained more prominence during the COVID-19 pandemic. For instance, according to an OECD assessment[[77]](#footnote-78) companies that have been taking “proactive steps to address the risks related to the COVID-19 crisis in a way that mitigates adverse impacts on workers and supply chains are likely to build more long-term value and resilience, improving their viability in the short term and their prospects for recovery in the medium to long term”.[[78]](#footnote-79) Moreover, good knowledge of company’s supply chains can reveal its dependencies on particular supplier, material or region that can prevent disruptions in its operation and increase resilience.

* **Operational efficiency, costs savings and innovation, research and development**

Research shows that companies which incorporate ESG factors into their policies generate higher returns, albeit each industry is affected differently by ESG factors[[79]](#footnote-80). For instance, relative resource efficiency (the amount of energy, water, and waste used in relation to revenue) is significantly correlated (95-99% confidence) with financial performance in sectors as diverse as food products, chemicals, pharmaceuticals, automotive, and semiconductors. (See Annexure IV of Supporting study on due diligence, p. 81, Table 13, rows 2 and 3).

Evidence shows that an environmentally friendly corporate policy results in better operational performance (OECD p. 9). Including ESG issues in their sustainability framework leads to cost savings for companies through innovation, resource efficiency, and revenue enhancements due to sustainable products[[80]](#footnote-81). Other researchers found in approximately 176 different sources evidence to support the claim that solid ESG practices result in better operational performance[[81]](#footnote-82). Environmental topics such as pollution abatement, resource efficiency and corporate environmental management practices in general are often mentioned as the most relevant to operational performance (OECD report, Annex C p. 39).

Whelan and Fink provide several examples of companies which have benefitted economically from resource and process efficiencies due to their sustainability programs. For example, they cite the company Dow which has invested 2 billion USD since 1994 in improving resource efficiency but in return has saved 9.8 billion USD from reduced energy, waste and water consumption. Another example is Wal-Mart, which increased its fleet efficiency and saved almost 11 million USD due to improved fuel efficiency[[82]](#footnote-83) .

McKinsey found evidence that increased efficiency in the use of resources is correlated with better financial performance. Those companies that performed best in each sector were also those which had the most ambitious sustainability strategies.[[83]](#footnote-84)

In a 2012 report on sustainability for consumer business companies, Deloitte concludes that sustainability is recognised increasingly as a primary **driver for strategic product and business model innovation**. The report argues that **truly innovative companies have put sustainability at the heart of their business**, examining strategic decisions based on the criterion of sustainability (Supporting study on due diligence, p. 315). Another study from the same year[[84]](#footnote-85) explains that sustainability-driven innovation is about improving business operations and processes to become more efficient and reduce costs, and also about insulating a business from the risk of resource price shocks and shortages, which can all together provide significant economic benefits[[85]](#footnote-86).

As regards **science-based targets specifically, 63% of companies say their science-based targets drive innovation** and 55% of companies claim to have gained competitive advantage from science-based targets[[86]](#footnote-87). Several studies assess how operational costs would be reduced as a result of switching to low-carbon technologies which companies need to invest in to mitigate their adverse climate impacts. According to the estimations of the UK Committee on Climate Change [The Sixth Carbon Budget – The UK's path to Net Zero](https://www.theccc.org.uk/wp-content/uploads/2020/12/The-Sixth-Carbon-Budget-The-UKs-path-to-Net-Zero.pdf) from December 2020 (figure 3), by 2050, savings in operating costs are likely to be larger than the investment requirements.[[87]](#footnote-88) CDP Europe’s study on [Doubling down Europe's low carbon investment opportunity from February 2020](https://www.cdp.net/en/research/global-reports/doubling-down) covered 882 European companies and concluded that **emissions reduction initiatives typically yield cost savings in excess of the initial investment** **at an average profit of EUR 17 per tonne of CO2.**

* **Access to public contracts and procurement by other companies**

Companies undertaking due diligence in the value chains may have better access to public procurement contracts. Following the implementation of EU Directives on public procurement, a number of Member States (e.g. Denmark, Ireland) have also included due diligence requirements in their national public procurement frameworks[[88]](#footnote-89). Similarly, one could expect that SMEs that have sustainability practices are more likely to be contracted by large companies transitioning to more sustainable operations given that this will lead to cost savings with regard to the information gathering and easier compliance for the large company, while SMEs not keeping up with the transition efforts of large companies may lose business opportunities.

* **Benefits deriving from harmonisation**

In the survey conducted for the Supporting study on due diligence, the majority of stakeholders indicated that mandatory due diligence as a legal standard of care may provide potential benefits to business relating to harmonization, legal certainty, a level playing field, and increasing leverage in their business relationships throughout the supply chain through a non-negotiable standard.

Moreover, levelling the playing field may get extra boost to the frontrunners to go a step further in their sustainable business approach.

* Other benefits identified through the application of the French due diligence law

In addition to the studies mentioned above, the **report evaluating the application of the French due diligence law**[[89]](#footnote-90) confirms **mid-to long-term competitiveness benefits** resulting from the French law and finds that the following elements increase the competitiveness of French businesses subject to the law vis-à-vis companies that are not under its scope (the list is not complete, benefits mentioned above are not reiterated here):

* A **better knowledge of the supply chain and its environment** is an opportunity contributing to increased competitiveness.
* A better knowledge of suppliers and the entire value chain results in **better commercial relationships**. When the company knows its supply chain better, it is possible to find and establish **balanced conditions that are advantageous for both parties in the longer term**.
* Sustainable value creation results in **more trust in the company**. With growing interest and expectations of potential **workers**, **consumers** and **civil society**, a company with sustainable operations will be preferred. In the same vein, good sustainability performance will provide a competitive advantage when it comes to **choosing the company as a supplier, for investment/access to capital or any other commercial relationship**.

### Analysis of which company is likely to benefit more from the regulatory initiative

On the basis of the above, the following **conclusions** can be made about the benefits of the legislation, **without taking into account the differences in the cost impact at this stage**:

* All companies in the scope may derive performance benefits linked to, for example, operational cost savings due to more efficient operations, better risk management, better relationships with and trust from stakeholders, etc.
* Companies not subject to the scope but being part of the value chain of companies in scope may indirectly also benefit from more sustainable practices, sustainability investments and resulting efficiency gains, better performance, etc.
* Improved branding and reputational benefits, benefits arising from attracting talent, etc. arises less when a large number of companies are subject to the new rules, i.e. within the single market. However, as EU companies may be first movers in global markets, they may derive these benefits on those markets.
* Companies with more advanced sustainability risk and impact management may derive less benefits regarding operational performance, operational efficiency, access to capital, more resilience, etc. but may benefit from cost savings linked to harmonisation, increased level playing field, etc.
* Companies with less advanced sustainability risk and impact management may derive more benefits from better risk management, efficiency gains, better stock price performance, more resilience, better productivity, more innovation than those that are already frontrunners.
* Large companies facing significant transition risks are likely to benefit more, than those that face less risks.
* SMEs not keeping up with the transition efforts of large buyer companies may benefit more by improving sustainable corporate governance and thereby securing business opportunities.
* Benefits related to cost of capital and financing are likely to increase over time in light of ongoing measures requiring proper sustainability risk management in banks and some other financial institutions and growing awareness about sustainability risks in the finance sector.

## Compliance costs for companies

### Estimations in the Supporting study on due diligence

The most significant cost implications under this initiative will be linked to the **corporate** **due diligence obligation**. For estimating the costs for businesses implied by such a duty, our starting point was the **Supporting study on due diligence** which relies on a **thorough literature review** (also integrating the authors’ findings regarding market practices and their regulatory review), as well as a **stakeholder survey involving 334 companies.** Due to the gaps in the responses from companies on cost estimations, the results of the survey were checked against some of the findings of related literature, particularly previous impact assessments of relevant policies (e.g. the EU and US conflict minerals regulations, the EU Timber Regulation, the EU Non-financial Reporting Directive, the EU Directive on the Protection of the Environment through Criminal Law and the Directive on the Control of Major-accident Hazards Involving Dangerous Substances).[[90]](#footnote-91)

The **survey** asked respondents about their perceptions on costs related to the human rights and environmental due diligence activities of their companies, including for the status quo and for two broadly-defined scenarios: one with **only new reporting obligations regarding due diligence covering the entire value chain**, and one with **mandatory due diligence rules covering the entire value chain and all – human rights and environmental – aspects of sustainability**.[[91]](#footnote-92) Survey respondents were requested to indicate estimations for the (monthly) **number of person-days** needed forthe following due diligence and reporting activities (separately or altogether):

1. Impact assessments and tracking effectiveness of actions
2. Training
3. Incorporation of standards into contracts / codes of conduct
4. Audits / investigations
5. Leverage (suppliers / investee companies / third parties) and collective engagement
6. Reporting activities.

Among others, the study calculates the increases in total annual costs of all due diligence activities under the “new reporting only” and the “mandatory due diligence” scenarios compared to the status quo. The calculations are based on the total **internal labour costs** (calculated from the person-day estimates for all activities)[[92]](#footnote-93), to which mark-ups for the **overhead costs** (25% of the internal labour costs) and for the **costs of** **outsourced activities or external services** such as audits and experts (17% of the internal labour costs under the “new reporting only” scenario and 25% under “mandatory due diligence”) are added. The percentages used for these mark-ups are based on the responses received in the survey to a separate question requesting estimations for the **various cost elements** related to all due diligence and reporting activities: cost of labour, overheads, cost of outsourcing, cost or reporting, other costs.[[93]](#footnote-94)

**The results of the survey have to be read with caution** because of the difficulties for stakeholders to estimate the costs, given the fact that the policy options assessed were not specified fully, and also due to the limited or lacking experience with due diligence activities of some respondents.[[94]](#footnote-95),[[95]](#footnote-96) Only a **limited** number of companies participating in the survey estimated the cost of due diligence under the various policy scenarios.[[96]](#footnote-97) Estimates provided by **companies which are already undertaking due diligence for human rights and environmental impacts in a more comprehensive manner** appear to be the **most reliable**.[[97]](#footnote-98)Therefore, the detailed calculations in the study **rely on these responses only**, despite the fact that the costs that they currently incur does not represent the “average” company of this size. However, **the overwhelming majority** of such companies in the sample are companies **with 1000+ employees** (which is also due to smaller companies being underrepresented among the survey respondents[[98]](#footnote-99)), and have very high annual revenues.[[99]](#footnote-100)

In the case of certain due diligence activities, **very** **large differences were detected between mean and median values**, in the entire sample as well as within company size groups. In order **to account for outliers in the data, the study uses median values**. Still, due to the gaps in available data for companies with less than 1000 employees[[100]](#footnote-101), the study uses the values indicated by companies with 50-1000 employees to calculate the costs for SMEs (defined for the purposes of the assessment as companies with up to 250 employees), and it uses the estimates given by companies with 1000+ employees also for calculating the costs for middle-ground companies that have 250 to 1000 employees. The study then **scales the estimates according to companies’ revenues** to account for the size effects within these two company size groups, even though this methodology, combined with the lack of sufficient data, will result in a **structural break** in the estimates (see the highest revenue tranche of SMEs and the lowest revenue tranche of large companies in the following table).

The results for **increases in the total firm-level annual costs** of due diligence activities under the mandatory due diligence scenario **compared to the status quo** are summarised in the study as follows:[[101]](#footnote-102)

|  | | **Revenue**  (in EUR) | **Increase in annual costs**  (in EUR) |
| --- | --- | --- | --- |
| **Large companies (with more than 250 employees) with revenue of:** | 50 billion | | 4 696 100 |
| 10 billion | | 939 200 |
| 1 billion | | 93 900 |
| 100 million | | 9 400 |
| **SMEs (up to 250 employees) with revenue of:** | 50 million | | 69 400 |
| 25 million | | 34 700 |
| 10 million | | 13 900 |
| 1 million | | 1 400 |

It is important to note the following points with regard to the survey results:

* The figures presented above represent **incremental costs compared to the status quo for companies already undertaking human rights and environmental due diligence**, as explained above. **For companies not yet undertaking due diligence**, or not yet covering the full spectrum of possible adverse impacts (or the impacts required by the policy option assessed), **the increases in costs would be higher**.
* The estimations do not yet take into account that, in the future, companies would be under more pressure to improve their practices even in the absence of new reporting rules and mandatory due diligence, due to **further increasing expectations** of investors, customers or other stakeholders, competitive pressure, evolving jurisprudence or as a result of other new EU-level or national laws.[[102]](#footnote-103) Thus, **the average burden implied by this initiative could be somewhat smaller if** not **compared** to the status quo but **to the dynamic baseline** in which such developments are likely to increase businesses’ due diligence costs to some extent.
* **The survey did not inquire about one-off (initial) costs**, e.g. for training staff, the set-up of IT solutions, and initial risk assessments.[[103]](#footnote-104) The EU Conflict Minerals Regulation’s and the NFRD’s Impact Assessments (2013) are referred to in the study as calculating with EUR 13 500 total initial costs and EUR 5 000 initial training costs, respectively, for the large companies falling under the scope of those measures, simply concluding that the initial costs for a due diligence initiative would be higher.
* Respondents were *not* specifically asked to provide estimates about the possible cost of transforming value chains. Thus, the cost estimates of the Supporting study **only capture the cost of setting up and operating due diligence processes** but **do not include the (one-off) costs related to rearrangements of companies’ value chains**.[[104]](#footnote-105)
* Nevertheless, in the context of one-off costs, the authors point out the possibility for businesses to spread the transitional financial burden on businesses over several years. They also refer to the need to consider initial costs as “investments” that are anyway needed to ensure the sustainable operation of the company itself, e.g. to prevent that reputational risks reduce the value of the company.
* **Cost estimates vary substantially even within the groups** of companies formed according to their **size**. The study points out that the **cost implications would vary according to other individual characteristics of the companies** as well, such as their business models, the degree of internationalisation, the size, complexity and location of their supply chains, the number of their customers (consumer and B2B), their place in the value chain, their scope of exploitation of economies of scale, their operational processes (e.g. employee-intensive vs automation), the degree of software utilisation for corporate and value chain management, etc., which are, however, difficult to control in the research. Furthermore differences are also attributable to the **sectors** in which the companies are active.
* **The impact of factors that diminish the compliance cost of individual companies**, such as cost sharing among companies by cooperating through industry alliances (where for example the alliance conducts investigations or collects information, etc.) in the same sector or value chain and the use of innovative technologies are not quantified and as such **not taken into account in the firm-level compliance cost estimations** in the study (such factors will be discussed in the next section).
* Finally, the costs for individual companies also depend on the extent to which others in the supply chain are conducting due diligence according to the required standard. The study points out (p. 443) that **compliance costs, including in particular for SMEs, would be significantly lower if all companies in the supply chain were to exercise appropriate due diligence** as they would mainly need to focus on their own risks.

Estimations in other relevant literature

Once these data were collected, we analysed other international academic **literature**, grey literature and literature on national initiatives available with a view to filling in the data gaps and comparing cost estimations to improve the robustness of the analysis. All of the studies gathered were scrutinized for:

1. relevance for the initiative: to what extent are the due diligence requirements comparable to the underlying initiative (thus meaning comparable data);
2. quality of the data: to what extent are the data included in the study valid and robust;
3. up-to-date information: to what extent are the data up-to-date and still relevant.

After the selection process, the following **six sources** matched these three criteria sufficiently:

* CEPS’ [Study on the Non-Financial Reporting Directive](https://op.europa.eu/en/publication-detail/-/publication/1ef8fe0e-98e1-11eb-b85c-01aa75ed71a1/language-en/format-PDF/source-220119255), prepared for the European Commission to support the review of the NFRD, November 2020
* the Commission’s [Impact Assessment SWD(2021)150 accompanying the Proposal for the Corporate Sustainability Reporting Directive](https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52021SC0150&from=EN), April 2021;
* The Commission’s [Impact Assessment Report SWD(2020)335 accompanying the Proposal for a Regulation concerning batteries and waste batteries](https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A52020SC0335), December 2020;
* Study for the OECD by the University of Columbia’s School of International Public Affairs on [Quantifying the Costs, Benefits and Risks of Due Diligence for Responsible Business Conduct – Framework and Assessment Tool for Companies](https://mneguidelines.oecd.org/Quantifying-the-Cost-Benefits-Risks-of-Due-Diligence-for-RBC.pdf), June 2016;
* Blome C., [Stopping conflict minerals with the OECD Guidance for responsible mineral supply chains: Status Quo in Europe](http://sro.sussex.ac.uk/id/eprint/65452/1/__smbhome.uscs.susx.ac.uk_tjk30_Documents_BlomeHofmannSchleper%20-%20Stopping%20conflict%20minerals%20with%20the%20OECD%20guidance%20for%20responsible%20mineral%20supply%20chains.pdf), University of Sussex, April 2016;
* [Economic assessment on due diligence along global supply chains](https://research.handelsblatt.com/assets/uploads/Studie_BMZ_Lieferkettengesetz.pdf) conducted for the German Ministry for Economic Cooperation and Development by Handelsblatt Research Institute (HRI) in July 2021.[[105]](#footnote-106)

As the Impact Assessment Report on Batteries and the OECD report are identical, they will be analysed jointly. In the same vein, the Commission’s impact assessment prepared for the CSRD relies on estimations of the 2020 CEPS study on the NFRD.

The elements that were examined in the studies were:

1. the difference between costs for SME’s and for non-SMEs, as most of the studies differentiated between these groups,
2. the difference between one-off costs and yearly recurrent costs: some studies only focus on recurrent costs, given that the assumption is that the one-off costs are relatively small compared to the recurrent costs, and for a significant number of the companies covered this is already a sunk cost (because they already have some form of information gathering process in place;
3. the specific elements or activities that were included in the analysed process (training of staff, external support from consultants or lawyers, gathering information, analysing information, auditing and reporting).

The literature review shows that, similarly to the authors of the Supporting study on due diligence, **other researchers and** **organizations also have difficulties with quantifying, let alone monetizing, the costs and benefits** of due diligence measures.

Comparing the studies is not obvious, given the different dimensions in the scope (specific sectors/products, specific types of companies, etc.), the design of the studies (based on interviews with a small(er) sample of companies versus larger, broader surveys) and the requirements covered by the study (the entire OECD framework versus specific requirements regarding a limited number of risks). However, **there are some common cost elements** in the studies, which we will compare at the end of our costs assessment, and that most of the studies have **broad ranges for the cost estimates**.

**There are multiple reasons for the broad cost ranges**: (1) some tasks and activities are **difficult to disentangle**: where does the information gathering end and where does the data analysing or tracking of effectiveness of the steps taken start? (2) **the difficulty for businesses to estimate** the costs in case they do not yet have any due diligence and/or sustainability reporting system in place; (3) the difficulty to distinguish costs that arise because of this initiative from costs that the company would anyway incur under the baseline scenario (business as usual or BAU) or have already incurred (sunk costs).

These six sources will be used to fill in the data gaps and adjust the costs assessment of the Supporting study on due diligence to the context and the content of this initiative. We will rely mainly on the NFRD study of CEPS / CSRD impact assessment and the OECD report / Batteries impact assessment for data on reporting costs under the revised rules, for estimating one-off costs, IT costs, and for demonstrating the expected broad range of the transition costs, as these instruments are closest to the general due diligence duty requiring attention on a wide range of human rights and environmental impacts and as they require comparable initial costs. For quantifying the cost sharing impact on firm-level cost reductions we will take the results of the Conflict minerals study as a basis. At the end, we will also compare the findings of these studies with our results derived mainly from the stakeholder consultation conducted in the Supporting study on due diligence.

### Factors mitigating compliance costs for companies

#### Cost sharing opportunities

Industry initiatives have a massive potential in **cost sharing** among companies that operate **in the same sector** or **have the same supplier**. Literature identifies joint industry initiatives as factors that can significantly reduce the cost of due diligence.[[106]](#footnote-107)

Bayer and de Buhr (2011) analyse the effects of Section 1502 of US Dodd-Frank Act[[107]](#footnote-108) on companies. They refer to **joint industry initiatives**, e.g. the **creation of common platforms for information collection, tracking, reporting and auditing**, to reduce the labour efforts and cost burden on companies, as reducing the possible negative impact on companies’ relative loss in competitiveness (Supporting study on due diligence, p. 316).[[108]](#footnote-109)

The study of the University of Sussex (2016) on cost and benefits of implementing due diligence policies regarding conflict minerals estimated the potential cost reductions based on a survey: a quarter of the 29 EU-based companies surveyed estimated that **sectoral collaboration could reduce the costs by 25 to 50%**. A further quarter of them even estimated that the potential cost savings **could amount to 50 to 75% of recurrent costs**.[[109]](#footnote-110)

In the same vein, total costs emerging in relation to the value chain would be lower than the costs calculated for companies individually in case there are **several EU companies sourcing from the same supplier**. This may be particularly relevant for SMEs as they often purchase from the suppliers that are already under scrutiny due to being part of the supply chain of other – larger – companies as well. However, as the Supporting study (p. 430) points out, the overlaps of business relationships could result in costs savings for any company that cooperates with others for instance in risk assessments. An indirect form of cooperation is the **use of specialised companies for conducting audits for many firms**, which can also result in reducing the costs for individual companies.

Finally, additional significant cost reductions can be expected from **cross-sectoral cooperation**, for instance for those aiming at scaling up the exploitation of the potentials in circular economy: innovations ensure that the waste of one sector is used as raw material by another sector, resulting in mutual benefits and improved compliance with due diligence obligations to reduce negative environmental impact.[[110]](#footnote-111)

#### Modern technologies

The Supporting study on due diligence elaborates on the **potential offered by digitalisation and new technology tools to provide unprecedented solutions to identify, address and eliminate human rights infringements and environmental challenge**.[[111]](#footnote-112) Modern **tracking and surveillance technologies** (for instance using satellites, drones, radars, smart sensors like radio-frequency identification, smart dust, big data, blockchain, and platform-based solutions) can drastically reduce the cost of data gathering, on-site audits, monitoring and impact mitigation. Moreover, advanced tracking systems are not only emerging but are also becoming cheaper, which has also been fuelled by harmonisation of standards in the field.[[112]](#footnote-113) The Supporting study **projects a significant rise in the utilisation of these, more and more low-cost technologies**, including by SMEs and even micro businesses. The study also points to the **likelihood of new EU regulation spurring innovation** in new technologies and software solutions, for instance the emergence of platform-based companies offering audit-based **data collections**, **data management**, hazard recognition and early-warning systems, or companies providing primary data on the basis of on-site audits.

Important cost savings could arise via **automation of contracts**[[113]](#footnote-114) (both B2B and B2C applications) and from a more systematic **use of important European digital data assets** such as the Copernicus satellite data[[114]](#footnote-115) for the monitoring of such contracts, or Airbus Starling[[115]](#footnote-116) satellite data services to monitor sustainability objectives. Such services can be made **available to SMEs at very low cost**. **Artificial intelligence and machine-readable public disclosures** of other companies in the value chain will also help make data collection and assessment more efficient.

Own assessment of firm-level direct compliance costs arising from the due diligence obligation

As explained above, the most significant cost implications under this initiative will be related to the corporate due diligence obligation. **This section will quantify and monetize, to the extent possible, the substantive compliance costs and the administrative (reporting) costs incurred by companies directly as a result of such an obligation.** We will assess the **firm-level costs** for the various types of companies that will be covered by the various policy options to different extent, then aggregate the costs for the corporate sector for the different policy options.

When calculating **firm-level compliance costs**, we will **rely in the first place on the Supporting study on due diligence**. However, the survey for the study had been conducted before the details of the policy options of this initiative were developed, and there are some inconsistencies in the cost estimations for the various company size groups caused by the lack of availability of sufficient and comprehensive data from survey respondents. Therefore, in order to find more relevant data for assessing the policy options under this initiative, **we repeated some of the calculations on the basis of the raw data of the survey** (not published but made available for the Commission). We also had a closer look at the **components of the estimates**, in particular the costs of the various activities to allow for comparing the results to the baseline of this initiative. We then complemented our assessment by **an additional desk research** to see if data gaps can be filled in, and to compare the results with the outcome of other research in similar matters, including more recent studies.

#### Substantive compliance costs

The compliance costs will primarily comprise the **substantive compliance costs** with the due diligence obligations. This consists of two main parts:

* **Procedural due diligence costs**, i.e. the **costs of establishing and operating the due diligence processes and procedures**. These costs include, first of all, the cost of **impact mapping and tracking**: **collecting** data to initially identify actual and potential adverse impacts in the company’s own operations and in its value chains, **analysing** such information, **monitoring** the development of such impacts and **tracking the effectiveness** of actions taken to reduce adverse impacts where such impacts have been identified.[[116]](#footnote-117) Costs will also be implied by the need to build **leverage** over the supply chain (for example through contracts), possibly also by taking part in **collective engagement**, and to incorporate human rights and environmental sustainability standards in **contracts** with suppliers and other business partners or to develop suppliers’ codes of conduct. These costs are **both one-off and recurring costs, which we will monetise**, taking the results of the Supporting study as a starting point;
* **Costs of transition to sustainability**, i.e. the **expenditures and investments** necessary to **change** the company’s own operations and support value chains in order to comply with **the duty to mitigate actual and prevent potential harm**. This is particularly relevant for companies that identify actual or potential adverse impacts. They will need to undertake **further steps** to enforce the contractual terms and standards enshrined in codes of conduct, to exercise the leverage over the value chain, possibly **to reorganise their upstream and downstream supply chains**. As a last resort, companies may need to terminate relationships with non-cooperative or non-compliant suppliers and switch to new suppliers complying with the required standards. Companies may also need to **adjust their production processes, products or services**. For instance, they may need to invest into climate-friendly or resource-efficient production processes, into research and innovation, into human capital, or upgrading facilities, etc. They may possibly even need to change their **business models**. Most of these costs constitute **one-off costs** but companies would not necessarily incur them immediately after the entry into force of the rules. Instead, they are likely to be **spread across several years**, in particular where the due diligence duty requires achieving a result through gradual implementation, for example in the case of climate change mitigation.[[117]](#footnote-118) As such costs **depend very much on the current individual circumstances of the individual companies** which are difficult to control, we will assess them **qualitatively with descriptive and qualitative examples to demonstrate** such effects, also based on other studies that estimate these costs within **broad ranges** for a limited due diligence duty.

The Supporting study monetised the costs of establishing and operating the due diligence processes and procedures. However, **some of the activities the costs of which have been included in these estimations will already result in impact mitigation**[[118]](#footnote-119). We will continue to include the costs of these due diligence activities in the monetised costs, even though parts of them could also be regarded as belonging to the transition costs.

Finally, it is to be noted that even though we have initially identified **litigation costs** as a separate type of cost that businesses may face, such costs are more likely to occur for companies that do not comply with the obligations.

The due diligence study found that there is no expectation of a floodgate of cases, as the evidence shows that human rights and environmental rights-based cases remain rare even when they are possible in substantive law because other hurdles to bringing such claims are still in place (legal costs which are usually not available to human rights victims, problems related to access to legal aid or lawyers, procedural and practical hurdles related to gathering of evidence, etc.). Even if this initiative improves access to remedy for victims, many of these hurdles are likely to remain unaddressed when the new law enters into force. Furthermore, **the more a company focuses on complying with the substantive due diligence obligations, the lower the risks that it would face litigation costs as a result of this regulation.** Therefore, there is little probability that litigation costs will arise as additional cost where the company has incurred all the compliance costs.

In practice, the French mandatory horizontal due diligence duty applying to very large companies and introducing liability so far resulted in only a few court cases[[119]](#footnote-120) which shows that the **litigation risk linked to such an instrument is relatively low**.

The open public consultation survey also gathered views about the expected impact: 70.3% of respondents indicated that an EU framework will lead to increased legal certainty about how companies should tackle their impact in the value chain. **The increased legal certainty is also likely to lower the risk of litigation for the companies complying with the due diligence obligation**. A small part of respondents feared increased legal uncertainty given the uncertainty as regards how the courts would treat certain claims. Moreover, once a claim arises a large portion of the respondents indicate that the **legal costs can be significant**. [[120]](#footnote-121)

Substantive cost of setting up and operating due diligence processes

The substantive compliance costs of due diligence will include **one-off** **(initial)** and **recurrent (annual) costs** in all policy options that are retained for a detailed assessment. The Supporting study inquired survey respondents only about recurrent costs. However, costs will likely be higher in the year(s) following the introduction of the due diligence obligation. Initial impact mapping and assessment, the training of current staff and familiarising with the new obligations, establishing cooperation arrangements with others in the same sector or in the supply chain, amending of existing contracts with suppliers etc. are all likely to imply higher costs initially.

The 2020 CEPS study on the NFRD (page 9) estimated on average the total administrative costs of non-financial reporting to **decrease by about 30% after the first year**. By analogy, we will rely on the estimations of the Supporting study for recurrent costs but we will count with an additional 30% for all due diligence activities as one-off costs. This may result in a slight overestimation of the costs for the first year during which both the recurrent costs and the one-off costs would arise (although one-off costs do not necessarily arise in the first year and thus, this additional bit could spread across a few years).

From the table summarizing the costs estimated in the study (see the relevant section above), we will use the following data:

* For **extremely large companies with more than EUR 5 billion turnover** we will use the Supporting study’s estimate for large companies (with more than 250 employees) with revenue of EUR 10 billion: **EUR 940 000**. In the EU, there are approximately 150 companies with a turnover between EUR 5 and 10 billion, and an additional 150 with a turnover above EUR 10 billion according to the Orbis database.
* For **all other** **large companies**, i.e. those with less than EUR 5 billion turnover, which is the overwhelming majority, the Study’s estimate for large companies (with more than 250 employees) with EUR 1 billion revenue will be used: **EUR 94 000** as an average figure.[[121]](#footnote-122)
* For **SMEs**, including **listed (non-micro) small companies** and **all medium-sized companies**, the Study’s estimate for SMEs (companies with 10 to 250 employees) with a revenue of EUR 25 million will be used for the detailed calculations: **EUR 34 700**. Taking into account that under the Accounting Directive medium-sized companies are associated with a net turnover between EUR 8 to 40 million, that the **average turnover** of non-listed medium-sized companies is around **EUR 16 million** and that the average turnover of listed SMEs is **EUR 12 million**[[122]](#footnote-123), this will probably result in an **overestimation** of the compliance costs for companies of this size.[[123]](#footnote-124)

The following table summarises the one-off and recurrent costs for the different-sized companies, compared to the status quo for companies that are already undertaking a certain level of due diligence across all human rights and environmental issues:

|  |  |  |  |
| --- | --- | --- | --- |
|  | SMEs | Large companies with less than EUR 5 bn turnover | Large companies with EUR 5 bn+ turnover |
| Recurrent costs in EUR | 34 700 | 94 000 | 940 000 |
| One-off costs in EUR (30% of recurrent costs) | 10 400 | 28 200 | 282 000 |

It is worthwhile to note that under the Supporting study’s survey, **IT costs and expense related to the purchase and implementation of other technological solutions** needed to conduct due diligence (e.g. the cost of impact tracking technology) are only taken into account to the extent they are part of the costs of outsourced activities and overheads (the remaining part of the costs, making up two-thirds of the total, only cover internal labour costs). The study suggests that the **recurring** part of these costs are indeed included in the cost estimations but initial **one-off** costs should be considered additionally. Other studies estimating due diligence costs also calculated with setting up IT systems as a separate one-off cost item. However, as we calculated one-off costs by proportioning them to the total recurrent costs based on the ratio CSRD estimates, the resulting figures should **already include** the initial investment needs that are related to introducing the necessary technological systems or IT upgrades. Therefore, there is no need to correct the estimates for this reason.

The impact assessment of the **Batteries** proposal calculated for **setting up the necessary IT systems with a one-off costs EUR 36 000 to 90 000**. This range applies to the about **50 large** batteries and vehicle manufacturers that would be required to do supply-chain due diligence for raw materials in industrial batteries, and also includes the installation and support costs (i.e. internal labour costs or outsourced activities). Our cost calculations for such large companies are **comparable** to these figures.

**As a next step, we will adjust the Study’s cost estimations** to take into account **the differences in the level of due diligence currently** undertaken by the companies and, at the same time, to compare **the incremental costs implied by this initiative to the dynamic baseline** of the initiative (instead of the status quo at the time of conducting the survey). This requires an adjustment for business as usual and, for the companies also under the scope of the sustainability reporting obligation of the CSRD proposal, a deduction of reporting and other overlapping – data gathering and analysis – costs (for companies that will not be subject to the CSRD, reporting costs will be deducted from the total substantive costs and will be indicated separately as administrative costs). Afterwards, we will also account for the cost mitigation factors (such as joint industry initiatives and the use of modern technologies) which are not reflected in the study’s estimates but are likely to reduce the costs incurred by all companies under the scope. Finally, we will calculate the cost of a simplified due diligence duty (relevant for certain company groups in some of the policy options).

1. Business as usual (BAU)

**Business as usual (and sunk) costs** are particularly relevant in the case of companies that already have a due diligence systems in place. According to the Supporting study’s survey, for about **two-thirds** of very large companies (with more than 1000 employees) and **one-third** of medium-sized and middle-ground companies (with 50 to 1000 employees), undertaking some kind of due diligence for human rights or the environment is part of their existing corporate practices and governance.[[124]](#footnote-125)

**The estimates** from which the costs were calculated in the Supporting study **were received from companies that already undertake due diligence activities** for at least some impacts and would continue to do so without a legal obligation, even if this is limited (e.g. stop at tier 1 suppliers). Therefore, these estimates should be adjusted to take into account that the level of due diligence currently undertaken by the “average” company under the scope of this policy initiative is lower. To avoid an **underestimation** of the compliance costs for the “non-experienced” companies, it seems appropriate to count with **larger initial (one-off) costs** for this group of companies as their costs would be higher initially. In addition, incremental **recurrent costs** are also higher for them.

At the same time, **many companies which do not specifically undertake human rights and environmental due diligence have social and/or environmental information gathering and risk management processes** in place. These are needed **to comply with their obligations under existing legislation** related to health and safety requirements of products, or under environmental, social (such as in posting of workers) or anti-corruption law, environmental law or to voluntarily comply with the EMAS Regulation (EU Eco-Management and Audit Scheme). Even though such schemes (other than the product safety-related ones) may not extend to the value chain, companies can still build on them when complying with the new due diligence requirements; **supplementing already existing processes costs less that establishing new ones.** Thus, **the increase in costs should remain limited**.[[125]](#footnote-126)

It is also to be noted that the **incremental costs implied by this initiative should be compared to the dynamic baseline** of the initiative. However, the survey in the Supporting study compared the additional costs to the status quo in a static manner and has therefore **not calculated with newly emerging, national or EU level requirements** that would already prompt companies to undertake some of the activities that a due diligence obligation would also require (e.g. because of increased interests of banks under the revised CRD/CRR, German due diligence law and its impact on the value chains in another Member State, synergies with the EU deforestation proposal, impact of the Fit for 55 package on own operations, etc.). Therefore, the overall estimations in the study are **likely to overestimate the incremental compliance costs, in particular for the large companies**.

Based on all these considerations, we find it appropriate to account for the lower average level of due diligence practices in the dynamic baseline scenario by increasing the estimates by 5% for large companies (i.e. by 15% for one-third of large companies) and by 20% for the SMEs (i.e. by 30% for two-thirds of SMEs), based on own assessment:[[126]](#footnote-127)

|  |  |  |  |
| --- | --- | --- | --- |
| BAU  (SME: 120%, large: 105%) | SMEs | Large companies with less than EUR 5 bn turnover | Large companies with EUR 5 bn+ turnover |
| Recurrent costs in EUR | 41,640 € | 98,700 € | 987,000 € |
| One-off costs in EUR | 12,490 € | 29,600 € | 296,100 € |

1. Reporting costs

In the baseline, **large companies and listed SMEs** (excluding micro undertakings) will be covered by the revised non-financial reporting (sustainability reporting) rules according to the new CSRD. As the estimates in the Supporting study include **the cost of reporting, this should be deducted** for such companies.

On the other hand, **medium-sized non-listed companies will have to incur the cost of public disclosure under the sustainable governance initiative**. These costs have already been taken into account in the Supporting study’s cost estimates (as the costs of “reporting activities”). However, as these are not part of the substantive compliance costs, we will deduct this cost element from the estimates here and **show it separately as administrative costs** in a separate section.[[127]](#footnote-128)

We will approximate the amount that should be deducted from the total cost estimate of the Supporting study as cost of **reporting** by using the ratio of “reporting activities” in the total of person-days calculated based on the average of the most reliable estimates received in the survey of the Supporting study (raw data)[[128]](#footnote-129)is 10%.[[129]](#footnote-130)

The following table shows the cost of the “reporting activities” and the total costs without the cost of “reporting activities”:

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Cost of DD activities (in EUR) | Ratio in total costs | SMEs | Large companies with less than EUR 5 bn turnover | Large companies with EUR 5 bn+ turnover |
| **Reporting activities** | 9,8% |  |  |  |
| recurrent |  | 4,090 € | 9,700 € | 96,900 € |
| one-off |  | 1,230 € | 2,900 € | 29,100 € |
| **Total costs without "reporting activities" (in EUR)** |  |  |  |  |
| recurrent |  | **37,550 €** | **89,000 €** | **890,100 €** |
| one-off |  | **11,270 €** | **26,700 €** | **267,000 €** |

1. Cost-mitigating factors

In this section we will **quantify the potential cost savings** that may arise due to the use of **modern technologies and other opportunities to reduce firm-level costs by cost sharing** (such as joint industry initiatives, value chain cooperation and cross-sectoral collaboration) discussed on the basis of the literature review in the section on cost mitigation factors above.

These modern technologies as well as cost sharing cooperation are emerging and have not been accounted for in the cost estimates of the Supporting study. They are projected to become available at decreasing price even for small companies. From literature it appears that for some impact and product types half of the companies would count with a cost reduction factor between 25% and 75%. Even though technology and other cost sharing possibilities may affect the costs of the various due diligence activities to different extent (e.g. modern technology could decrease the costs of impact mapping and tracking and cooperation could reduce the cost of exercising leverage), these cost mitigating factors are also interlinked (e.g. modern technologies will also be used by external auditors hired by several companies or sectoral cooperation could help develop surveillance technologies) and they are relevant to some extent to the entire due diligence process. Therefore, **we will apply a single, average cost mitigating factor to the overall substantive compliance costs** (without the reporting costs).

Following a **cautious approach**, we will apply the lower-end estimate from the above-mentioned study: a 25% reduction factor. As a result, the substantive cost of compliance with the corporate due diligence obligation is the following:

|  |  |  |  |
| --- | --- | --- | --- |
| Cost mitigating factors (-25%) | SMEs | Large companies with less than EUR 5 bn turnover | Large companies with EUR 5 bn+ turnover |
| Recurrent costs in EUR | 28,160 € | 66,800 € | 667,600 € |
| One-off costs in EUR | 8,450 € | 20,000 € | 200,300 € |

1. Further overlaps with the CSRD: data gathering and analysis

The overlap with the CSRD proposal goes beyond the strictly speaking “reporting activities”. The administrative activities necessary to comply with the sustainability reporting rules will **partly overlap** with the activities that companies need to do to comply with the substantive due diligence obligations. More particularly, companies will already be expected to be **collecting data** in a more structured manner regarding all their adverse impacts throughout the value chains and to **analyse** these data in order to make a materiality assessment and identify their significant impacts as they will need to report on them. Even though this may not amount to the extent and depth of data gathering and analysis that would be required under the due diligence obligation (setting a clear obligation to identify and address the adverse impacts and track the effectiveness of impact mitigation measures, etc.), and data gathering and analysis attributed to the CSRD will extend beyond adverse impacts and due diligence-related matters such as corruption, tax), we **estimate that at least half** of the these types of activities conducted for complying with the reporting rules also contribute to complying with the due diligence obligations.[[130]](#footnote-131) In order to avoid double counting, **the overlapping compliance costs already accounted for under the CSRD proposal should be deducted** from the estimated costs implied by this initiative for those companies which will fall under both regimes.[[131]](#footnote-132)

Regarding these **other cost elements overlapping** with the CSRD (beyond the actual reporting activities), we rely on the 2020 CEPS study on the NFRD[[132]](#footnote-133) which distributes the total administrative costs of complying with the non-financial reporting obligations across the following types of activities:

* retrieving data: 24% (internal costs, including labour costs and overheads: 19%, external costs 5%),
* analysis of information: 22% (internal: 12%, external: 10%),
* reporting information: 32% (internal: 12%, external: 20%),
* other costs: 22% (internal: 10%, external: 12%).

We assume that the first two items (which we will cluster as **data gathering and analysing activities**) **will make up 46% of all administrative costs under the revised sustainability reporting rules (CSRD)**, too.[[133]](#footnote-134) Taking into account the average firm-level annual (incremental) administrative costs estimated by the CSRD proposal’s impact assessment (p. 210-211) for **reporting against EU sustainability reporting standards**, our due diligence cost estimates for companies under the scope of both initiatives should be decreased by the following amounts (from the costs of “**Impact assessments & tracking effectiveness of actions”** and **“Audits / investigations”**, which we will treat together as “data gathering and analysing” here as well):

|  |  |  |  |
| --- | --- | --- | --- |
| Overlapping CSRD compliance costs | **listed SMEs** (reporting against a standard) | **middle-ground** companies with 250-500 employees that are **listed**, are banks or insurance companies (about 9 700 such EU companies), and  **other large non-listed EU companies** (about 35 200 such companies)[[134]](#footnote-135) | **large companies with min. 500 employees** that are listed or are banks or insurance companies (less than 2000 such EU companies)[[135]](#footnote-136) |
| **CSRD costs:** | | | |
| recurrent (in EUR) | 22,700 € | 63,500 € | 105,700 € |
| one-off (in EUR) | 9,300 € | 22,700 € | 43,430 € |
| *Comment:* |  | *It seems reasonable to use this figure for large companies with less than EUR 5 bn revenue in this assessment.* | *It seems reasonable to use this figure for companies with EUR 5 bn+ revenue or more in this assessment.* |
| Half of all CSRD data gathering and analysis cost (23% of total costs): | | | |
| recurrent (in EUR) | 5,220 € | 14,600 € | 24,300 € |
| one-off (in EUR) | 2,140 € | 5,200 € | 10,000 € |

Calculating the ratio of the costs of the various due diligence activities[[136]](#footnote-137) the same way as the cost ratio of “reporting activities” above[[137]](#footnote-138) (but comparing to the total cost excluding the “reporting activities” – except for the case of non-listed medium-sized companies as they are not under the scope of the CSRD proposal), we arrive at the following substantive compliance costs, as per activity, for the various company size groups:

| **Substantive costs per activity (full DD):** | **non-listed medium-sized companies** | **listed SMEs** | **Large companies with less than EUR 5 bn turnover** | **Large companies with EUR 5 bn+ turnover** |
| --- | --- | --- | --- | --- |
| **Training** | *11,7%* |  |  |  |
| recurrent | 3,300 € | 3,300 € | 7,800 € | 78,000 € |
| one-off | 990 € | 990 € | 2,300 € | 23,000 € |
| **Data gathering and analysis** (incl. impact assessment & tracking effectiveness of measures, and audits & investigations)[[138]](#footnote-139) | *58,5%* |  |  |  |
| recurrent | 16,470 € | 11,250 € | 24,400 € | 366,000 € |
| one-off | 4,940 € | 2,800 € | 6,500 € | 107,000 € |
| **Incorporation of standards into contracts / codes of conduct** | *23,1%* |  |  |  |
| recurrent | 6,500 € | 6,500 € | 15,400 € | 154,000 € |
| one-off | 1,950 € | 1,950 € | 4,600 € | 46,000 € |
| **Leverage** (suppliers / investee companies / third parties) **& collective engagement** | *6,7%* |  |  |  |
| recurrent | 1,890 € | 1,890 € | 4,500 € | 45,000 € |
| one-off | 570 € | 570 € | 1,300 € | 13,000 € |
|  |  |  |  |  |
| **Total substantive compliance costs**  **(full DD):** | *100,0%* |  |  |  |
| **recurrent** | **28,160 €** | **22,940 €** | **52,200 €** | **643,000 €** |
| **one-off** | **8,450 €** | **6,310 €** | **14,800 €** | **190,000 €** |

1. Simplified (targeted) due diligence

Depending on the policy option retained for detailed analysis, certain companies will only need to comply with **targeted due diligence rules**, focusing on the most relevant adverse impacts in the sector concerned as identified for them in legislation. This would imply **lower substantive compliance costs**. In some of these policy options, the targeted obligation would apply only to medium-sized and midcap companies (horizontally in all sectors). Under a thematic approach even large companies would be concerned; however, in that option the firm-level costs would be even lower as only one (or a few) adverse impact types would be covered by the measure.

We will **assume that a more targeted due diligence requirement will only imply 75% of the cost increase estimated for the full due diligence duty**. This seems to be a cautious approach but it is to be recalled that this is an average estimation. To verify for the robustness of this estimation, we compared the resulted costs with the cost estimations of the deforestation and conflict minerals proposals which contain such a “relevant risk only” approach. The result of this comparison shows that calculating with a 75% of overall cost impact compared to the horizontal duty’s overall cost impact would not result in an underestimation of the costs.

For many larger companies a targeted regime (e.g. under the thematic due diligence) could even result in very low additional costs or to no cost increase at all, as two-thirds of them (according to the Supporting study’s survey) are already doing due diligence for at least some impacts and adding new impact categories to existing processes imply substantially less costs that setting up new due diligence systems. On the other hand, if companies today cover mainly their tier 1 suppliers, an obligation extending to their entire value chain may result in more significant additional costs than adding new risks to existing processes.

We will use the following adjusted costs for the cost of compliance with the **targeted due diligence obligation** (these figures already take into account the factors of cost mitigation as calculated in the previous point):

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| ***Substantive costs (targeted DD):*** | **non-listed medium-sized companies** | **listed SMEs** | **Large companies with less than EUR 5 bn turnover** | **Large companies with EUR 5 bn+ turnover** |
| *recurrent* | 21,120 € | 17,210 € | 39,100 € | 482,000 € |
| *one-off* | 6,340 € | 4,730 € | 11,100 € | 143,000 € |

Substantive costs of transition to sustainability

A potentially large part of these transition costs can be regarded as **investments into the sustainability transition**. The due diligence duty – and the clarified directors’ duties – will generate investments in particular into climate and nature-friendly operations and value chains. It is difficult to estimate how much an individual company will need to invest as it depends on its risks, impacts and preparedness.

Furthermore, the investments needed to comply with this initiative could also bring important **benefits, including short-term cost reductions** (such as operational cost reductions, efficiency gains, or other benefits),which could **counterbalance compliance costs in some cases already in the short-term, but in most cases over a mid to longer time horizon**. For example, one study examines 181 ways of preventing waste generation in chemical plants, and finds that only one of them “resulted in a net cost increase”. In other words, process innovation more than offsets costs in 180 out of 181 cases.[[139]](#footnote-140)

Looking at the consequences for the company of switching to key low-carbon technologies, the cost of this have recently fallen and is expected to continue falling. Zero-emission technologies are set to become **cheaper than the high-carbon alternatives.** Such technologies may also result in **operational cost savings**. In fact, **investments into low-carbon processes are expected to pay back fully in the short, medium or long term.** By 2050, savings in operating costs are likely to be larger than investment requirements for all major types of low-carbon investments[[140]](#footnote-141) but investments into climate neutrality can even pay back in a relatively short period of time.[[141]](#footnote-142) In this context, science-based targets often **drive innovation** and are deemed to be a source of competitive advantage.[[142]](#footnote-143),[[143]](#footnote-144) For many other environmental investments, and especially for sectors depending directly from the quality of nature, the **benefits will also be derived from restoring services that nature provides**[[144]](#footnote-145), or **from reducing the use of raw materials** and thereby improving operational performance[[145]](#footnote-146).

**Box: Cost of transition to zero-emissions is decreasing, low-carbon investments are becoming profitable**

The biggest driver of **cost reductions** and technological improvement will be through deployment at scale. For instance, due to reduced technology costs and reduced cost of capital over the last decade, the generation of electricity from offshore wind has now the same cost as electricity from a new gas-fired power plant. Batteries, like renewables, are commercialised at scale and have become significantly cheaper in recent years. This trend has also been apparent internationally: mass manufacture and deployment of solar panels, onshore wind turbines and batteries have reduced costs. Recent reductions in costs, especially of renewable electricity generation and batteries, mean that **zero-emissions technologies are set to become cheaper than the high-carbon alternatives.** A large chemical company informed that their plan to achieve their net zero target by 2030 for low carbon electricity will be achieved largely at net zero cost.

As explained above, evidence shows that investments into climate neutrality can reduce costs, as energy efficiency, clean energy and alternative energy sources can reduce operational costs[[146]](#footnote-147). A CDP Europe report from 2020[[147]](#footnote-148) shows the **business case for low-carbon investments**. According to the study covering 882 European companies, **emissions reduction initiatives typically yield cost savings in excess of the initial investment at an average profit of EUR 17 per tonne of CO2[[148]](#footnote-149).[[149]](#footnote-150) Companies also identified new revenue opportunities from low-carbon goods and services – more than six times the investment needed to realize them.** Furthermore, investments into climate neutrality can pay back in a relatively short period of time. As an example, ENEL plans to invest EUR 16.8 billion in onshore wind and solar by 2023, promising to raise core earnings by 13%[[150]](#footnote-151).

The magnitude of such transition costs will vary to a large degree, also depending on the sector and activities of the company, the number of suppliers, the location of its operations and supply chains, etc. Accordingly, any quantitative estimate would result in a very **broad range** for transition costs, even within the various company size categories.

As this cost element was not part of the supporting study, we checked other studies. The impact assessment of the **batteries initiative** (building on the OECD report) calculated with an annual cost of **EUR 12 500 to 365 000** for “**carrying out due diligence and reporting**”. This is a **very broad range** and estimates the costs of a comprehensive supply chain due diligence and reporting for 50 large companies limited to a particularly risky product.

#### Administrative costs

An additional element of compliance costs beyond process related and transition costs is linked to reporting to the public as this constitutes an important step of due diligence. At the same time, this initiative will **not imply any incremental administrative costs for the companies covered by the CSRD**: they will already incur such costs when they comply with their sustainability reporting obligations (including the disclosure of information on the company’s adverse impacts and the due diligence measure taken to address them).

**For the companies not subject to this public reporting regime**, the cost of reporting to the public should, in principle, be considered administrative costs. Accordingly, such costs will be borne by **non-listed medium-sized companies** to the extent they are covered by the policy options. The following administrative costs will apply, which will need to be added to the total substantive compliance costs for the companies concerned (for an explanation of the numbers, see later):

|  |  |
| --- | --- |
| **Administrative costs (upper bound)** | **Non-listed medium-sized companies** |
| **Full due diligence** |  |
| Recurrent | €4,090 |
| One-off | €1,230 |
| ***Targeted due diligence*** |  |
| *Recurrent* | *€3,066* |
| *One-off* | *€920* |

Even though they are not subject to the scope of the proposal, **the CSRD impact assessment estimated** the total recurrent administrative costs also for non-listed SMEs: reporting in a non-standardised manner would annually cost **EUR 11 000**, the one-off costs would be **EUR 5 500**. The relatively lower costs estimated above reflects that fact that the CSRD costs also contain data gathering and analysis costs (as shown above). Also, under the sustainable corporate governance initiative medium-sized companies would need report to the public **only about the matters governed by this initiative, in a simplified manner**.

#### Comparative assessment of compliance costs

The following table summarizes the compliance costs for the various company groups (without taking into account the transition cost, which we did not attempt to quantify):

| **Total direct incremental compliance costs of mandatory DD (without transition costs):** | **Non-listed medium-sized companies** | **Listed SMEs** | **Large companies with less than EUR 5 billion turnover** | **Large companies with EUR 5 billion turnover** |
| --- | --- | --- | --- | --- |
| **Full due diligence** |  |  |  |  |
| recurrent | 32,250 € | 22,950 € | 52,200 € | 643,000 € |
| one-off | 9,700 € | 6,300 € | 14,800 € | 190,000 € |
| ***Targeted due diligence*** |  |  |  |  |
| *recurrent* | *24,200 €* | *17,200 €* | *39,100 €* | *482,000 €* |
| *one-off* | *7,250 €* | *4,750 €* | *11,100 €* | *143,000 €* |

Considering the scope and content of the policy options assessed for this initiative, mainly the following firm-level cost estimates will be used to aggregate the business sectors’ direct compliance costs:

| **Company-level direct incremental compliance costs of mandatory DD (without transition costs), in EUR:** | **Recurrent costs** | **One-off costs** |
| --- | --- | --- |
| **Micro LLCs,**  **Non-listed small LLCs,**  **Non-listed medium-sized LLCs not in high-impact sectors** | Not covered, only indirect costs | |
| **Listed SMEs (full due diligence)** | 22 950 | 6 300 |
| **Medium-sized non-listed LLCs in high-impact sectors subject to the simplified due diligence obligation** | 24 200 | 7 250 |
| **Midcap LLCs (“moderately” large) in high-impact sectors subject to the simplified due diligence obligation** | 39 100 | 11 100 |
| **Large and very large companies (including midcaps where subject to full due diligence obligation)**  **(larger number estimated for the about 300 largest LLCs)** | 52 200 – 643 300 | 14 800 – 190 300 |

For **non-listed medium-sized companies and listed SMEs** this means, on average, additional recurrent costs of about **0.09 to 0.10% of their revenue**, taking into account that the basis of the detailed calculations was the Supporting study’s cost estimates for SMEs with a revenue of EUR 25 million. For **large companies** (including midcaps and very large companies), this ratio is about **0.004 to 0.006%** (calculating with the cost estimates for large companies with an average revenue of 1 billion, and 10 billion for the 300 very large companies).

In the table below, the results of the four studies are deconstructed for the purposes of **comparison**. This has to be read with caution as the scope and size of these initiatives differ, and because the incremental compliance costs under this initiative already take into account that the CSRD would apply in the baseline scenario. At any rate, the comparison confirms that **our cost estimates**, which were are on a very small sample of companies and which have been adjusted to reflect better the evolving circumstances and the policy options currently assessed, **fall within a range comparable with the estimations of other relevant research**.

|  |  | **Own estimates based on DD Supporting study**  **(full DD)[[151]](#footnote-152)** | **CSRD IA / CEPS Study on NFRD** | **Batteries IA / OECD report** | **Blome – Stopping Conflict minerals** |
| --- | --- | --- | --- | --- | --- |
| Training | SME | € 3 300 (recurrent)  € 1 000 (one-off) |  |  | €18 000 (recurrent)  €8 000 (one-off) |
| Non-SME | € 7 800 – 78 100 (recurrent)  € 2 300 – 23 400 (one-off)[[152]](#footnote-153) |  |  | €306 000 (recurrent)  €81 000 (one-off) |
| Setting up systems and procedures | SME | € 8 400 (recurrent)  € 2 500 (one-off)  (incl. incorporating standards into contracts / code of conduct, leverage and collective engagement) |  | € 3 150 – 100 000 (one-off – compliance policies and supply chain operating procedures)  +  € 36 000 – 90 000 (one-off – IT systems) | €10 000 (one-off – legal advice) |
| Non-SME | € 19 900 – 199 000 (recurrent)  € 6 000 – 59 700 (one-off) |  | € 100 000 – 205 000 (one-off – compliance policies and supply chain operating procedures)  +  € 36 000 – 90 000 (one-off – IT systems) | €15 000 (one-off – legal advice) |
| Data gathering and analysis | SME | € 11 250 – 16 450 (recurrent)[[153]](#footnote-154)  € 2 800 – 4 950 (one-off)  (incl. internal and external audits and investigations, impact assessments, tracking effectiveness of actions, in addition to the costs incurred under the CSRD) | € 5 200 (recurrent)  (incl. data collection and data analysis)  € 2 150 (one-off) | € 12 600 – 72 000 (recurrent – data collection and verification)  +  € 13 500 – 22 500 (recurrent – external audits) | €20 000 (recurrent)  €13 000 (one-off)  (external audits)  + included in reporting |
| Non-‑SME | € 24 400 – 366 000 (recurrent)  € 6 500 – 107 000 (one-off)  (in addition to the costs incurred under the CSRD) | € 16 500 (recurrent)  € 6 800 (one-off) | € 12 600 – 72 000 (recurrent – data collection and verification)  +  € 90 000 (recurrent – external audits) | €80 000 (recurrent)  €102 000 (one-off)  (external audits)  + included in reporting |
| Reporting | SME | For non-listed:  € 4 100 (recurrent)  € 1 250 (one-off)  For listed: no additional costs calculated due to overlap with scope of CSRD | € 3 650 (recurrent)  € 1 500 (one-off)  (reporting activities)  Total cost of sustainability reporting against a standard (incl. all other cost listed in the table, except the cost of assurance):  EUR 22 700 (recurrent)  EUR 9 300 (one-off)[[154]](#footnote-155) | € 12 500 – 365 000 (recurrent – together with the cost of carrying out due diligence) | €16 000 (recurrent) |
| Non-SME | No additional costs calculated due to overlap with scope of CSRD | € 11 500 (recurrent)  € 4 700 (one-off)  (reporting activities)  Total cost of sustainability reporting against a standard:  € 63 500 – 105 700 (recurring);  € 22 700  – 43 430 (one-off)[[155]](#footnote-156) | € 12 500 – 365 000 (recurrent – together with the cost of carrying out due diligence) | € 139 000 (recurrent)  € 1 000 (one-off) |
| Other | SME |  | € 2 500 (recurrent)  € 1 050 (one-off) |  | € 2,000 (recurrent) |
| Non-SME |  | € 7 900 (recurrent)  € 3 200 (one-off) |  | € 1,000 (recurrent) |
| **Transition (mitigation) costs** | SME |  |  | €12 500 – 365 000 (recurrent – cost of carrying out due diligence and reporting) |  |
|  | Non-SME |  |  | €12 500 – 365 000 (recurrent – cost of carrying out due diligence and reporting) |  |
| **Total** | SME | € 22 950 – 32 250 (recurrent)  € 6 300 – 9 700 (one-off) | N/A | €  39 150 – 190 000 (one-off)  € 38 600 – € 459 500 (recurrent) | € 37,000 (recurrent without auditing)  € 18,000 (one-off without auditing)  € 57,000 (recurrent with auditing)  € 32,000 (one-off with auditing) |
| Non-  SME | € 52 200 – 543 300 (recurrent)  14 800 – 190 300 (one-off) |  | € 136 000 – 295 000 (one-off)  € 115 100 – 527 000 (recurrent) | € 485,000 (recurrent without auditing)  € 168,000 (one-off without auditing)  €565,000 (recurrent with auditing)  € 270,000 (one-off with auditing) |

At the end of our assessment, we also cross-checked our results with the results of **the recent** [**economic assessment on due diligence along global supply chains**](https://www.bmz.de/resource/blob/92544/18fbb046bf85f95c5b07731ff69c4600/studie_BMZ_lieferkettengesetz.pdf) **conducted for the German Ministry for Economic Cooperation and Development by Handelsblatt Research Institute (HRI) in July 2021**. This assessment is based on the survey of 331 randomly selected corporate decision-makers and then, in a second survey, targeted 87 companies all of which are in favour of legal regulation in Germany.

**The results the German survey show that the business costs of training (employees and suppliers), or regular reporting requirements are limited.** Looking at the randomly selected companies with fewer than 250 employees (i.e. SMEs) that already had experience with supply chain management in accordance with the United Nations' requirements, more than 70% said that this did not require a full-time position.

The randomly selected companies (including SMEs) put the expected **annual cost** of due diligence compliance along supply chains at an average of **EUR 81 300**. The companies favouring the mandatory due diligence, estimate the average annual costs at **EUR 165 200**. However, there are a few outlier companies that (expect to) spend comparatively large amounts on their supply chain management, which pushes the average up. On average (median), the expected costs are between **EUR 3 000 and 5 000** given by the companies (including SMEs) randomly selected in the survey and **EUR 5 400 to 6 000** for those favouring the law. However, the German supply chain law **focuses on human rights violations** and addresses environmental harm only to limited extent, therefore the costs of a full corporate due diligence duty is definitely higher for companies operating in sectors where the risk of adverse environmental impact is high.

#### Analysis of which company is likely to incur higher or lower compliance cost as a result of this regulatory initiative

The broad estimates of businesses participating in the survey of the Supporting study on due diligence and other similar studies (e.g. the 2020 CEPS study on the NFRD) reflect the fact that direct – but also indirect – compliance costs will differ according to sectorial and individual company characteristics.

* Companies active **in several sectors** of the economy or **offering a broad range of products or services** are likely to face higher compliance costs. Companies in **certain sectors**, for instance those offering financial services and retail services are likely to bear relatively significant costs as their value chains may extend to almost any other sectors (see also the Supporting study on due diligence, p. 428).
* Companies with **a business model** building on, for example, the provision of the **lowest cost goods** or **high-speed delivery** that places pressure on warehouse workers, or on **land use in countries where ownership rights may be contested**, etc. are likely to incur more costs.
* Companies with **more business partners, longer and more complex value chains, in particular if located in third countries presenting higher risks,** are likely to incur higher compliance costs.
* The costs are expected to be lower for **companies that rely on suppliers which themselves carry out sustainability due diligence**. This is more likely if the value chain is located in the EU or in a third country where social and environmental standards are high.
* Smaller companies (subsidiaries or value chain partners) that are not under the scope of the initiative would bear **higher trickle down costs** in case they operate in high-impact sectors or are selling their products or services, directly or indirectly, to larger companies operating in high-impact sectors. However, large companies will be expected to share the burden with their suppliers, so it will be in the best own interest of the large company to share information or cooperation platforms, etc. with its suppliers which in turn could lower the cost for anybody else in the chain.

### Own assessment of aggregated direct compliance costs for companies arising from the due diligence obligation

To get the total compliance costs for all companies under the scope of the various policy options, we will **multiply the average firm-level compliance costs** (substantive costs and, where relevant, administrative costs) **by the number of companies of the given size category** covered by the scope.[[156]](#footnote-157)

For the number of companies covered, we primarily rely on the Orbis database but we also use data from the 2020 CEPS study on the NFRD, in particular for the number of listed SMEs. The tables in Annex 13 summarise for each option how many companies would be covered by the full and by the targeted due diligence obligation from each company category (size, listing).[[157]](#footnote-158) In this section we will summarize in a **table for each option** the **number of companies covered** from each company type (size, plus listed or not), the **content** of the due diligence obligation applying to them (full vs. simplified or more targeted) the **estimated aggregated recurrent and one-off costs** per such company groups (using the relevant firm-level cost estimate), and the total aggregated compliance cost estimated for the option concerned.

It needs to be stressed that our cost calculations should be understood as being of an **indicative nature**: the number of companies covered by the individual options are approximated using mainly the Orbis database and they depend a lot on the definition of the company size categories.

Option 1a: sectoral approach

The costs will depend primarily on the sector or sectors to be covered, including whether it is limited to a certain subsector or even to an activity (1, 2 etc. digit NACE code) and how many companies have their primary activity in that sector. We used the example of C13 Manufacture of textiles (NACE code: C13).[[158]](#footnote-159) For a few sectors, the Supporting study on due diligence gave first estimations about the cost impacts, however, we not only have adjusted those cost calculations in this assessment but will also apply them only to the given size categories of limited liability companies.

| **Option 1a: example for a sectorial approach – C13 subsector Manufacture of textiles**  (full DD in the specific (sub)sector) | | | | | |
| --- | --- | --- | --- | --- | --- |
| **Type of LLCs under scope** | **Number of LLCs under scope** | out of which: | | | |
| **Non-listed medium-sized companies** | **Listed SMEs** | **Large companies with less than EUR 5 bn turnover** | **Large companies with EUR 5 bn+ turnover** |
| **Large** (50+ empl. and €8m+ turn., excl. medium-sized)[[159]](#footnote-160): | **385** |  |  | 135 | 15[[160]](#footnote-161) |
| recurrent |  |  |  | 18,087,300 € | 24,767,050 € |
| one-off |  |  |  | 5,128,200 € | 7,326,550 € |
| **Medium-sized non-listed** (50-250 empl. and €8m-40m turn.): | **650** |  |  |  |  |
| recurrent |  | 20,962,500 € |  |  |  |
| one-off: |  | 6,292,000 € |  |  |  |
| **Listed non-micro SMEs:** |  |  |  |  |  |
| recurrent | **30** |  | 688,200 € |  |  |
| one-off |  |  | 189,300 € |  |  |
| **Total costs:** | **1,065** |  |  |  |  |
| **recurrent** | **64,500,000 €** |  |  |  |  |
| **one-off** | **18,900,000 €** |  |  |  |  |

Option 1b: thematic approach

The cost of this approach obviously depends on how many adverse impact types the initiative covers, and on the selected impact or impacts (e.g. how salient they are in the biggest sectors of the economy etc.), even though this affects the cost estimates less than the sectoral coverage in Option 1a. While certain adverse impacts are more likely to be present in some sectors, we assume a general reduction of the due diligence costs for all companies in all sectors, calculating with 40% of the simplified due diligence rules for one impact type (for example child labour).

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Option 1b: Thematic approach**  **(rough estimation for DD focusing on one impact type[[161]](#footnote-162), covering all sectors)** | | | | | |
| **Type of LLCs covered** | **Number of LLCs covered** | out of which: | | | |
| **Non-listed medium-sized companies** | **Listed SMEs** | **Large companies with less than EUR 5 bn turnover** | **Large companies with EUR 5 bn+ turnover** |
| **Large** (50+ empl. and €8m+ turn., excl. medium-sized): | **24,120** |  |  |  |  |
| recurrent |  |  |  | 373,021,200 € | 57,897,600 € |
| one-off |  |  |  | 107,092,800 € | 17,127,600 € |
| **Listed non-micro SMEs:** | **1,410** |  | 1,410 |  |  |
| recurrent |  |  | 9,706,440 € |  |  |
| one-off |  |  | 2,667,720 € |  |  |
| **Non-listed medium-sized** in high-impact sectors (50-250 empl. and €8m-40m turn.) (70%): | **19,880** |  |  |  |  |
| recurrent |  | 192,358,880 € |  |  |  |
| one-off |  | 57,731,520 € |  |  |  |
| **Total:** | **39,670** |  |  |  |  |
| **recurrent** | 632,984,120 € |  |  |  |  |
| **one-off** | 184,619,640 € |  |  |  |  |

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Option 2: only very large companies with 1000+ employees** | | | | | |
| **Type of LLCs covered** | **Number of LLCs covered** | out of which: | | | |
| **Non-listed medium-sized companies** | **Listed SMEs** | **Large companies with less than EUR 5 bn turnover** | **Large companies with EUR 5 bn+ turnover** |
| **Very large** (1000+ employees) |  |  |  | all sectors & full DD | |
| Number | **8,910** |  |  | 8,610 | 300 |
| **Aggregated compliance costs:** | | | | | |
| **recurrent** | **642,432,000 €** |  |  | 449,442,000 € | 192,990,000 € |
| **one-off** | **184,518,000 €** |  |  | 127,428,000 € | 57,090,000 € |

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Option 3a: very large companies full DD in all sectors, midcaps and medium-sized only in high-impact sectors targeted DD** | | | | | |
| **Type of LLCs covered** | **Number of LLCs covered** | out of which: | | | |
| **Non-listed medium-sized companies** | **Listed SMEs** | **Large companies with less than EUR 5 bn turnover** | **Large companies with EUR 5 bn+ turnover** |
| **Very large** | (500+ empl. or 350m+ turn.) |  |  | all sectors & full DD | |
| Number | **23,290** |  |  | 22,990 | 300 |
| Aggregated compliance costs: | | | | | |
| recurrent | 1,393,068,000 € |  |  | 1,200,078,000 € | 192,990,000 € |
| one-off | 397,342,000 € |  |  | 340,252,000 € | 57,090,000 € |
| **Midcaps and medium-sized** (70%) | (50-500 employees and €8m-350m turn) | high-impact sectors & targeted DD | | |  |
| Number | 32,700 |  |  |  |  |
| *out of which medium-sized (50-250 empl. and €8m-40m turnover)* | *20,110* | ***19,880*** | ***230*** |  |  |
| *out of which midcaps:* | *12,590* |  |  | ***12,590*** |  |
| Aggregated compliance costs: | | | | | |
| recurrent | 977,754,000 € | 480,897,200 € | 3,958,300 € | 492,898,500 € |  |
| one-off | 285,165,700 € | 144,328,800 € | 1,087,900 € | 139,749,000 € |  |
| **Total:** | **55,990** |  |  |  |  |
| **recurrent** | **2,370,822,000 €** |  |  |  |  |
| **one-off** | **682,507,700 €** |  |  |  |  |

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Option 3b: fewer very large companies subject to full DD** (compared to option 3a) | | | | | |
| **Type of LLCs covered** | **Number of LLCs covered** | out of which: | | | |
| **Non-listed medium-sized companies** | **Listed SMEs** | **Large companies with less than EUR 5 bn turnover** | **Large companies with EUR 5 bn+ turnover** |
| **Very large** | (500+ empl. and €150m+ turn.) |  |  | all sectors & full DD | |
| Number | **9,360** |  |  | 9,060 | 300 |
| Aggregated compliance costs: | | | | | |
| recurrent | 665,922,000 € |  |  | 472,932,000 € | 192,990,000 € |
| one-off | 191,178,000 € |  |  | 134,088,000 € | 57,090,000 € |
| **Midcaps and medium-sized** (70%) | (50+employees and €8m+ turn. excl. very large) | high-impact sectors & targeted DD | | |  |
| Number | 34,640 |  |  |  |  |
| *out of which medium-sized: (50-250 employees and €8m-40m turn.)* | *20,110* | ***19,880*** | ***230*** |  |  |
| *out of which midcaps:* | *14,530* |  |  | ***14,530*** |  |
| Aggregated compliance costs: | | | | | |
| recurrent | 1,053,705,000 € | 480,897,200 € | 3,958,300 € | 568,849,500 € |  |
| one-off | 306,699,700 € | 144,328,800 € | 1,087,900 € | 161,283,000 € |  |
| **Total:** | **44,000** |  |  |  |  |
| **recurrent** | **1,719,627,000 €** |  |  |  |  |
| **one-off** | **497,877,700 €** |  |  |  |  |

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Option 4 : scope of CSRD proposal for full DD, simplified for high-impact non-listed mediums** | | | | | |
| **Type of LLCs covered** | **Number of LLCs covered** | out of which: | | | |
| **Non-listed medium-sized companies** | **Listed SMEs** | **Large companies with less than EUR 5 bn turnover** | **Large companies with EUR 5 bn+ turnover** |
| **Large**: | (Accounting Directive's definition) |  |  | all sectors & full DD | |
| Number | **65,040** |  |  | 64,740 | 300 |
| Aggregated compliance costs: | | | | | |
| recurrent | 3,572,418,000 € |  |  | 3,379,428,000 € | 192,990,000 € |
| one-off | 1,015,242,000 € |  |  | 958,152,000 € | 57,090,000 € |
| **Listed non-micro SMEs:** | (Accounting Directive's definition) |  | all sectors & full DD |  |  |
| Number | **1,410** |  | 1,410 |  |  |
| Aggregated compliance costs: | | | | | |
| recurrent | 32,345,400 € |  | 32,345,400 € |  |  |
| one-off | 8,897,100 € |  | 8,897,100 € |  |  |
| **Non-listed medium-sized** (simplified def.) (70%) | (50-250 employees and €8-40m turnover) | high-impact sectors & targeted DD |  |  |  |
| Number | **19,880** | 19,880 |  |  |  |
| Aggregated compliance costs: |  |  |  |  |  |
| recurrent | 480,897,200 € | 480,897,200 € |  |  |  |
| one-off | 144,328,800 € | 144,328,800 € |  |  |  |
| **Total :** | **86,330** |  |  |  |  |
| **recurrent** | **3,946,810,000 €** |  |  |  |  |
| **one-off** | **1,126,795,500 €** |  |  |  |  |

Finally, we summarize the results in a concise table:

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Aggregated direct business compliance costs (EUR)** | **Option 1a (e.g. C13 subsector)** | **Option 1b (one theme)** | **Option 2** | **Option 3a** | **Option 3b** | **Option 4** |
| **recurrent** | 60,000,000 | 630,000,000 | 640,000,000 | 2,370,000,000 | 1,720,000,000 | 4,090,000,000 |
| **one-off** | 20,000,000 | 180,000,000 | 180,000,000 | 680,000,000 | 500,000,000 | 1,170,000,000 |

### Indirect compliance costs for businesses

The due diligence obligation will also affect undertakings that are not directly subject to the legal requirements. On the one hand, business enterprises which are active in economic sectors where the risk of environmental or human rights harm is low are not likely to incur any substantial additional costs. On the other hand, **businesses which operate in high-impact sectors will be affected indirectly in case they are suppliers or subsidiaries of limited liability companies that are covered by the due diligence rules**.

According to the calculations based on the indicative list of high-impact sectors in Annex 11, about 30% of medium-sized and midcap companies in such sectors could be indirectly affected by the full due diligence obligation applicable to their parent companies as they are subsidiaries of such larger companies. These companies will incur indirect costs, but they have been taken out from the cost calculations for the high-impact group.

As regards value chain partners of companies subject to the full due diligence obligation, we calculate with the cost of targeted due diligence, although part of these companies will be indirectly affected by the due diligence obligation applying to the buyer company and therefore, in practice, may not bear all the additional costs of the targeted due diligence regime.

Smaller companies and business enterprises operating in legal forms other than limited liability companies, even if excluded from the scope of the legislation completely (except for listed small LLCs in some of the non-preferred options), will be involved in the impact mapping and mitigation in case they are in the value chain of companies covered directly by the legislation and will therefore incur some indirect costs.

It is **difficult to estimate the range of these indirect costs** and companies obliged to carry out due diligence will also be required to mitigate excessive burden on their SME suppliers. **Cost sharing** like joint industry initiatives and the use of **modern technologies** will **reduce the indirect compliance costs** as well. Furthermore, the planned **support measures and funds** to be mobilised would diminish the burden implied indirectly by the due diligence obligations.

### Additional direct cost of complying with directors’ duties

While directors’ duties would create some additional compliance costs for the companies, we will not calculate with additional **recurrent** costs, for the reasons explained in the main body of this assessment, and will only add minimal one-off costs: the cost of **setting up a risk management system** (EUR 2 500 for SMEs, EUR 5 000 for large companies) and the **external fee of validating science-based targets for GHG emission reductions** (EUR 5 000). The following table shows the calculations of the **additional cost arising in relation to compliance with directors’ duties:**

| **Company-level direct incremental on-off compliance costs of directors’ duties (EUR)** | **Option 1** | **Option 2a** | **Option 2b** | **Option 3** | **Option 4** |
| --- | --- | --- | --- | --- | --- |
| **Micro LLCs,**  **Non-listed small LLCs,**  **Non-listed medium-sized LLCs not in high-impact sectors** | €0 | €0 | €0 | €0 | €0 |
| **Listed (non-micro) SMEs, except:** | €2,500 | €2,500 | €2,500 | €2,500 | €7,500 |
| * *Number of such LLCs under scope* | 1,410 | 1,180 | 1,180 | 1,410 | 1,410 |
| **- medium-sized listed in high-impact** | - | €7,500 | €7,500 | - | - |
| * *Number of such LLCs under scope* | - | 230 | 230 | - | - |
| **- aggregated costs** | **€3,525,000** | **€4,675,000** | **€4,675,000** | **€3,525,000** | **€10,575,000** |
| **Medium-sized non-listed LLCs in high-impact sectors (100%)** | €2,500 | €2,500 | €2,500 | €2,500 | €2,500 |
| * *Number of such LLCs under scope* | 28,510 | 28,510 | 28,510 | 28,510 | 28,510 |
| **Medium-sized non-listed LLCs in high-impact sectors (70%, as under relevant due diligence scope)** | - | €5,000 | €5,000 | - | €5,000 |
| * *Number of such LLCs under scope* | - | 19,880 | 19,880 | - | 19,880 |
| **- aggregated costs** | **€71,275,000** | **€170,675,000** | **€170,675,000** | **€71,275,000** | **€170,675,000** |
| **Large companies** | €5,000 | €5,000 | €5,000 | €5,000 | €10,000 |
| * *Number of such LLCs under scope* | 65,040 | 65,040 | 65,040 | 65,040 | 65,040 |
| **Midcaps in high-impact sectors (def. as per DD option 3a)** | - | €5,000 | - | - | - |
| * *Number of such LLCs under scope* | - | 12,590 | - | - | - |
| **Midcaps in high-impact sectors (def. as per DD option 3b)** | - | - | €5,000 | - | - |
|  | - | - | 14,530 | - | - |
| **Very large companies in all sectors as per DD option 3 (i.e. larger than midcaps)** | - | €5,000 | €5,000 | - | - |
| * *Number of such LLCs under scope* | - | 23,290 | 9,360 | - | - |
| **1000+ employees** | - | - | - | €5,000 | - |
| * *Number of such LLCs under scope* | - | - | - | 8,910 | - |
| **- aggregated costs** | **€325,200,000** | **€179,400,000** | **€119,450,000** | **€44,550,000** | **€650,400,000** |
| **Total number** of companies incurring additional costs of **risk management:** | 94,960 | 94,960 | 94,960 | 94,960 | 94,960 |
| **Total** aggregated additional compliance **cost** of the **risk management duty:** | €400,000,000 | €400,000,000 | €400,000,000 | €400,000,000 | €400,000,000 |
| **Total number** of companies incurring additional costs of **science-based target setting:** | 0 | 55,990 | 44,000 | 8,910 | 86,330 |
| **Total** aggregated additional compliance **cost of the science-based target setting duty:** | €0 | €279,950,000 | €220,000,000 | €44,550,000 | €431,650,000 |
| **Total aggregated additional compliance cost of directors' duties** | **€400,000,000** | **€679,950,000** | **€620,000,000** | **€444,550,000** | **€831,650,000** |

### Aggregated costs for the preferred option

Finally, we sum up the aggregated compliance costs of the preferred option from both the corporate due diligence options (option 3a) and the directors' duties options (option 3):

|  |  |  |
| --- | --- | --- |
| **Preferred option: corporate due diligence option 3a & directors' duties option 3** | **Recurrent** | **One-off** |
| Cost of complying with the due diligence obligation (recurrent) | €2,370,822,000 |  |
| Cost of complying with the due diligence obligation (one-off) |  | €682,507,700 |
| Additional cost of complying with the directors’ duties (one-off) |  | €444,550,000 |
| **Total compliance costs:** | **€2,370,822,000** | **€1,127,057,700** |

Alternatively, the total compliance costs for options 3b (due diligence) and option 3 (directors’ duties) would be as follows:

|  |  |  |
| --- | --- | --- |
| **Preferred option: corporate due diligence option 3b & directors' duties option 3** | **Recurrent** | **One-off** |
| Cost of complying with the due diligence obligation (recurrent) | €1,719,627,000 |  |
| Cost of complying with the due diligence obligation (one-off) |  | €497,877,700 |
| Additional cost of complying with the directors’ duties (one-off) |  | €444,550,000 |
| **Total compliance costs:** | **€1,719,627,000** | **€942,427,700** |

## Impact on company-level competitiveness

The overall impact of the initiative on EU companies’ competitiveness in the EU and in global markets is the function of the compliance costs (including procedural and transition costs) and of the benefits implied by the initiative explained in the sections above. It is difficult to weigh the competitive disadvantages against the benefits for all companies: not only may estimations for costs (in particular transition costs) range across a broad spectrum but it is difficult to quantify the impact of beneficial factors on changes in the competitive position of a company in general.

*Sources of competitive advantages: more demand*

As the Supporting study on due diligence notes (p. 316), ”several recent studies highlight that **globalisation** of business and investment activities **has increased the demand for more transparent accounting of corporate responsibilities** **encompassing human rights, social, economic and environmental dimensions**. This demand has only increased with the Covid crisis, with the climate emergency and with the cost of inaction on environmental degradation becoming more immediate and tangible.

Consequently, the relative competitive advantage of proactive companies that engage in sustainability activities over other companies might have increased over time. However, the relationship between sustainability measures and competitiveness vary among different companies due to varying sectoral characteristics, including geography of markets and production, company size, role in business and value chains.

*Sustainability-linked product and process innovation as competitive advantage*

As explained in the benefits section as well, the main benefits of integrating the interests of stakeholders into corporate decisions have traditionally been better risk management (ie. avoiding fines, raw material shortages, supply chain disruptions, etc.), reputational benefits (attraction of talent, employee motivation, etc.) as well as efficiency gains/operational cost reductions (using less energy leading to cost savings, etc.). This has changed in recent years as explained in a recent PWC study: “sustainability is emerging as a **market driver with the potential to grow profits and present opportunities** for value creation — a dramatic evolution from its traditional focus on efficiency, cost, and supply chain risk”. In that respect, sustainable product innovation can have a substantial impact on a company’s revenues. As explained in the impact assessment report under drivers, a better focus on stakeholder interests and on the long-term interests of the company is likely to result in overcoming short-term financial pressures, engaging in investment and innovation, including product, production process and business model innovation. This assumption is in line with the results of a survey conducted on behalf of McKinsey & Company and the Canada Pension Plan Investment Board (CPPIB), in which 79% of C-level executives and board members state that they personally feel “pressure to deliver financial results in two years or less”. Tellingly, 86% of them note that this constraint is in contrast to their convictions, where they believe that using a longer time horizon to make business decisions would positively affect corporate performance in a number of ways, including strengthening longer-term financial returns and increasing innovation.

Research shows that such innovation and competitiveness benefits are most likely if sustainability is embedded in corporate governance through responsibility at the board level (ideally the CEO) and through clear sustainability goals that are measurable in quantity and time (target)[[162]](#footnote-163). Incorporating sustainability issues into the corporate governance framework, corporations will ultimately be able to realize cost savings through innovation, resource efficiency, and revenue enhancements via sustainable products, which ceteris paribus should lead to margin improvements[[163]](#footnote-164).

*Cost competitiveness*

However, for companies to be able to reap benefits, they should be able to absorb the costs of these requirements. The economic assessment on the expected impact of the German supply chain law concludes that, for the selected companies, the cost burden would reach 0.005 to 0.1% of their sales. For companies in favour of a supply chain law, which the survey addressed also separately, this ratio is between 0.06 and 0.6%. “This means that **implementation should be feasible even for small and medium-sized companies**, even if **the expense tends to decrease with company size**,” as the study concludes.

According to the Supporting study on due diligence, **the cost of mandatory due diligence compared to the revenue of companies appears to be relatively low**. As concerns the additional recurrent company-level costs as percentages of companies’ revenues, these costs on average amount to less than 0.14% for SMEs and 0.009% for large companies. These numbers are relatively low.

At the same time, these numbers represent average estimates and should be interpreted with caution. The cost estimates can **vary considerably between businesses because of different business models and market characteristics**, which will therefore **affect the competitive position of individual companies differently**. Differences across companies are even higher in terms of the **transition costs** related to changing the companies’ operations and value chains, which the study did not cover.[[164]](#footnote-165)

Therefore, due care was taken to minimise the risk of the cost impact affecting companies in such a way that their operations are compromised and their competitiveness is undermined through excessively high compliance cost, in particular when it comes to SMEs but also large companies (see in the impact assessment report under the comparison of the options/proportionality).

Regarding EU companies’ competitiveness in general, inclusion of non-EU importers above a certain size helps prevent competitive distortions in the EU single market. In global markets, EU companies could benefit from the first movers’ advantages too, i.e in addition to advantages liked to better risk management, efficiency gains, cost reductions, performance benefits liked to innovation. Namely, as market pioneers, EU companies could make pre-emptive investments in production capabilities by securing access to resources (e.g. suppliers, skilled personnel, etc.), technology (e.g. through patenting), secure market shares in global markets and gain economies of scale vis-à-vis later market entrants.

To sum up, the following conclusions can be made:

- while the cost imposed on companies is considerable, the intra-EU competitiveness of companies will not be affected significantly due to the large scope and horizontal character of the due diligence duty and through covering third country companies with an important turnover in the EU. While some benefits will not materialize due to the application of the duty to many, such as for example reputational benefits, others (cost reduction, operational efficiency, resilience, etc.) will arise. The cost impact has been reduced to a minimum with the very many elements ensuring proportionality of the options for SMEs (phase in, exclusion of small companies, support measures, only high impact medium covered, etc.)

- companies operating in global markets will see a negative impact on their cost competitiveness compared to third country competitors not subject to the due diligence duty. However, in the mid-to longer term, the benefits are expected to outweigh the costs and first mover advantages can also be exploited in global markets with significant additional benefits for the company

-in the mid to long-term, overall benefits are expected to outweigh the cost. This assumption is in line with the conclusion the report evaluating the application of the French due diligence law[[165]](#footnote-166) which confirms mid-to long-term competitiveness benefitsresulting from the French law

- the combined impact of due diligence, directors duties and remuneration is likely to lead to more benefits. Studies show that benefits are more pronounced if board is responsible and the company has a strategic orientation on sustainability. Furthermore, the considered complementary action on remuneration applying to all companies in the scope of the initiative would ensure that positive effects created by the other elements of the package would not be neutralised by non-aligned remuneration policies.

## Enforcement costs

The initiative will lead to additional **supervisory costs** for public authorities in the Member States as they will **monitor the implementation and enforce the corporate due diligence obligations**. We will attempt to monetise the supervisory costs in this section.

The assessment will **not count with additional costs for litigation, given that the magnitude of litigation is difficult to predict and** because the cost of court procedures are paid by the (civil) parties.

For the quantification of the supervisory costs for national authorities, **the impact assessment for the German bill on Supply Chain Due Diligence[[166]](#footnote-167) (which has similar objectives and instruments) was used as a starting point**. Given that the German draft law’s **scope is more restricted** (both with regard to the companies under its scope and the sustainability aspects covered), some assumptions were additionally made to calculate the costs by using the standard cost model.

The German assessment covered only large companies[[167]](#footnote-168), therefore, it would be incorrect to fully take the German cost into account when calculating the costs that public authorities will incur when enforcing the regulation for midcaps and (high-impact and/or listed) SMEs. We will calculate with **30% of the German ratio of the performed activities required per very large companies**. In addition, a reasonable assumption is that the time required to enforce the regulation **for** **SMEs amount to 20% of the time (and out-of-pocket costs) required for large companies**[[168]](#footnote-169), also taking into account that in most cases these will be subject to a targeted due diligence duty.

While the scope of this initiative would, in any policy option, be larger than the German bill, **the supervision will be risk-based**: authorities will have to focus on a systematic supervision of companies with the highest risks of adverse human rights or environmental impacts. In this context, supervisors will **review the information published by the company on its adverse impacts and due diligence** **annually** (disclosed to the public under the CSRD as part of the sustainability report or, in the case of non-listed SMEs, disclosed in accordance with the sustainable corporate governance legislative act) only with regard to **30%** of the companies under supervision. An additional **50%** of the disclosures will be subject to a **plausibility check**.

The enforcement costs take into account the following supervisory activities:

1. **Training:** In order to enforce the regulation, officials of the supervisory authority need specialized training that results in an additional labour cost. The training is organized per Member State, and therefore the activity is carried out 27 times.
2. **Review and plausibility check of information published on the company’s adverse impact and due diligence activities:** Under this item we categorize both the review and the plausibility checks of companies’ relevant documents.
3. **Reviewing companies as part of performing a risk-based control:** Some companies also need to be subjected to a risk-based control that involves a plausibility check of more information, a more in-depth review of the published report(s), reviewing the supply and value chain management of the company, and also requiring on-site inspections domestically or abroad.
4. **Initiation of administrative offense proceedings and dispatch of administrative fines:** this item refers to the costs of handling misdemeanour proceedings.

Based on the before-mentioned considerations, these activities will require the following time to complete:

| **Type of activity** | **Time required per activity (in minutes)** |
| --- | --- |
| **One-off (initial) costs:** |  |
| **Training (per Member State)** |  |
| Training | 6.960 |
| **Recurring (annual) costs:** |  |
| **Reviews and plausibility checks** |  |
| Reviewing reports | 120 |
| Plausibility check of reports | 360 |
| **Reviewing companies as part of performing a risk-based supervision** |  |
| Plausibility checks of information | 800 |
| In-depth review of reports | 480 |
| Review of value chain management (individual cases) | 2,400 |
| On-site appointments [inland] | 1,920 |
| On-site appointments [abroad] | 9,600 |
| **Initiation of administrative offense proceedings and dispatch of administrative fines** |  |
| Handling misdemeanour proceedings | 1.920 |

The general cost calculations apply to the systematic supervisory review of all companies under the scope. We will count with the number of large companies and SMEs (listed non-micro SMEs and/or medium-sized companies in high-impact sectors) as calculated in the option descriptions in Annex 13, summarized as follows:

|  |  |  |
| --- | --- | --- |
|  | Large | SME |
| Option 1a (sectoral) | 385 | 680 |
| Option 1b (thematic) | 24 120 | 21 290 |
| Option 2 | 8 910 | 0 |
| Option 3a | 35 880 | 20 110 |
| Option 3b | 23 890 | 20 110 |
| Option 4 | 65 040 | 21 290 |

Taking the above into account, we calculated the number of full-time equivalents[[169]](#footnote-170) needed to perform an activity once (if a one-time occurrence) or on a yearly basis (if the activity is recurrent) by using the following equation:

Subsequently, we used the average hourly wage in EU-27 (i.e. EUR 27.70)[[170]](#footnote-171) to determine the additional labour expenses related to the enforcement of the new corporate due diligence duty. Our calculations for the various scope options assessed are depicted in the following table:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Type of activity** | **Total additional labour costs in EU27 (in EUR)** | | | | |
| **Option 1b[[171]](#footnote-172)** | **Option 2** | **Option 3a** | **Option 3b** | **Option 4** |
| Training | €86,800 | €86,800 | €86,800 | €86,800 | €86,800 |
| Reviews and plausibility checks | €2,201,000 | €691,100 | €3,094,800 | €2,164,900 | €5,374,800 |
| Reviewing companies as part of performing a risk-based supervision | €3,296,300 | €1,034,900 | €4,634,800 | €3,242,100 | €8,049,300 |
| Initiation of administrative offense proceedings and dispatch of administrative fines | €1,886,600 | €592,300 | €2,652,700 | €1,855,600 | €4,606,900 |
| **Total recurrent:** | **€7,383,800** | **€2,318,300** | **€10,382,300** | **€7,262,600** | **€18,031,000** |
| **Total one-off (training):** | **€86,800** | **€86,800** | **€86,800** | **€86,800** | **€86,800** |

Member States will also be faced with other **expenses to which we refer as out-of-pocket costs (OOPC)**. These costs reflect actual expenses made by EU public authorities when performing certain activities. Keeping our assumptions in mind, we used the subsequent equation:

)

1. **Training:** Knowing that each training program implies an average OPCC expense of EUR 1 500, the total additional expenses related to the training of government officials will amount up to EUR 40 500 in the 27 Member States. Contrary to the other expenses, this cost only occurs once at the entry into force of the new rules.
2. **Plausibility checks and reviews of reports:** The calculations based on German impact assessment show that the OOPC of performing a plausibility check or a review of reports amounts to about one euro.
3. **Reviewing companies as part of performing a risk-based control:** In certain instances, supervisors will carry out on-site inspections. If this takes place inland, the public authority will face an actual OOPC expense of EUR 200 compared to EUR 4 000 if a foreign site is visited.
4. **Initiation of administrative offense proceedings and dispatch of administrative fines:** The OOPC of handling misdemeanour proceeding is approximately EUR 10.

In the following table we summarize the OOPC calculations for the various policy options:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Type of activity** | **Total additional Out-Of-Pocket Costs in EU27 (in EUR)** | | | | |
| **Option 1b[[172]](#footnote-173)** | **Option 2** | **Option 3a** | **Option 3b** | **Option 4** |
| Training | €40,500 | €40,500 | €40,500 | €40,500 | €40,500 |
| Reviews and plausibility checks | €8,500 | €2,700 | €12,000 | €8,400 | €20,800 |
| Reviewing companies as part of performing a risk-based supervision | €581,700 | €182,700 | €818,000 | €572,200 | €1,420,600 |
| Initiation of administrative offense proceedings and dispatch of administrative fines | €21,300 | €6,700 | €29,900 | €20,900 | €52,000 |
| **Total recurrent:** | **€611,500** | **€192,000** | **€859,900** | **€601,500** | **€1,493,400** |
| **Total one-off (training):** | **€40,500** | **€40,500** | **€40,500** | **€40,500** | **€40,500** |

To sum up the additional costs that the public authorities of the **27 Member States** will face each year in relation to enforcing the corporate due diligence obligation, we present the total costs in the next table as per option. Due to the necessary training, public authorities will also incur a **one-off cost of EUR 127 000 in total**.

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Total enforcement costs**  **in EU27 (in EUR)** | **Option 1b** | **Option 2** | **Option 3a** | **Option 3b** | **Option 4** |
| **Total recurrent:** | €7,995,300 | €2,510,300 | €11,242,200 | €7,864,100 | €19,524,400 |
| **Total one-off:** | €127,000 | €127,000 | €127,000 | €127,000 | €127,000 |

## Other economic impacts

**International competitiveness, trade, investment**

As explained in the problem definition, at macro-level, in the long term, a trend of decrease in CAPEX and investments in R&D as share of total revenues by companies might harm the level of productivity and the innovative capacity of the economy as a whole.

Although the cost of short-termism is difficult to monetise, preliminary estimates from McKinsey Global Institute suggest that short-termism may have cost the US economy the opportunity to generate an additional 5–6 million jobs over the past 15 years and over $1 trillion in unrealized GDP growth or 0.8% of GDP per year on average[[173]](#footnote-174).

As explained above, while EU companies might be at a relative disadvantage in cost competitiveness compared to non-EU companies in global markets, additional firm-level costs as percentages of companies’ revenues are relatively low. Therefore, no significant negative distortions for EU exporters that result from increased recurrent administrative cost are expected.

On the other hand, the new EU legislation will decrease distortions between EU and non-EU companies by creating more equal standards for EU companies, third country companies generating a high turnover in the EU as well as EU and non-EU suppliers. Furthermore, it will help increasing leverage with third parties in the value chain through the introduction of a “non-negotiable standard.”

As in the mid to long-term, corporate benefits are expected to outweigh costs (in terms of efficiency gains, better financial performance through innovation, etc.) and possibly also lead to first mover advantages in global markets (including securing access to resources, technology, secure market shares in global markets and gain economies of scale vis-à-vis later market entrants), the cumulative impact of these benefits is expected to lead to competitiveness gains for the economy.

Finally, better risk management, lower dependency on increasingly scarce natural resources, impact mitigation (for example climate change, biodiversity) and resulting resilience, including to sustainability-related shocks (e.g. climate change) will also contribute to positive overall impacts on the economy. Companies with unsustainable business models and practices will be driven towards switching to sustainable operations, value chains, products and services. All this will, in turn, also change the overall macro-economic environment: the initiative is expected to contribute to improving resilience and shock-absorbing capacity. Better corporate governance practices and clarified corporate and director duties will contribute to enhancing the reliability of sustainability-related information that companies disclose to the public and to investors. The initiative would therefore also help channel investments into sustainable companies and safeguard the economy’s growth potential

**Consumer prices**

The initiative could have an impact on prices for consumers if businesses endure increased compliance costs. However, consumers will be able to make better informed decisions given that they have increased certainty on the human rights and environmental impact of the production of the products they buy. The literature shows on the one hand that the impact on prices of sustainable corporate governance initiatives is fairly limited and even that a significant part of consumers is willing to pay a higher price for more sustainably produced goods. Furthermore, as explained under the international competitiveness and business performance, the investments that would be implied by the new duties are likely to reduce operational costs in the longer term, so the impact on consumer prices would not be substantial and can even be positive.

## Impacts on third countries and developing countries

Due to its global outreach via value chains, the sustainable corporate governance initiative will inevitably affect third country companies and economies. To date, it is difficult to assess the impact of partial or inadequate due diligence implementation, for standards that have been largely voluntary. Those that have been legislated[[174]](#footnote-175), are few, and not all have been in effect long enough to measure change on the ground. Based on the available data, reinforcing the respect of the environment and human rights throughout value chains of companies through mandatory due diligence obligations can have overwhelmingly positive impacts[[175]](#footnote-176) but may also have negative impacts, especially on developing nations and their businesses. I.e. while the human rights and environmental effects are expected to be overwhelmingly positive, the indirect economic impact through the value chain is likely to impose burden on third country companies in the value chain at least in the short-term.

Potential positive impacts include:

* Increased stakeholder awareness on key sustainability issues facilitating collaboration among companies, civil society organisations, governments and local communities to find lasting solutions that address both systemic and grassroots issues, including better access to remedy.[[176]](#footnote-177)
* Improved labour rights, human rights and environmental practices in developing nations that are in the supply chain of European companies through a more expansive approach to prevention and mitigation of harm by business. [[177]](#footnote-178)
* Increased adoption of international standards in developing nations.[[178]](#footnote-179)
* Improved political and social stability in the affected regions, which might be conducive to economic activity.[[179]](#footnote-180) [[180]](#footnote-181)
* Migration of regulatory standards in developing nations towards levels found in stricter jurisdictions, i.e. an ongoing “California Effect”, contributing to improved rule of law. [[181]](#footnote-182)
* Direct economic benefits for local communities[[182]](#footnote-183) i.e. increased trade opportunities and competitiveness for both European and third country companies as a result of responsible engagement and better business practices. [[183]](#footnote-184)
* Increased investments in sustainability domains incentivised by sustainability requirements[[184]](#footnote-185) as well as positive impacts on value chain companies (better financial performance, more innovation, etc.)[[185]](#footnote-186)
* Better access to remedy for victims of abuses
* Reduction of harmful practices and impacts on communities[[186]](#footnote-187) around production facilities directly affected by companies’ operations, and those indirectly affected by companies’ environmental footprint[[187]](#footnote-188).

Potential negative impacts include:

* Producers in developing countries moving to uncontrolled product markets due to increased cost of compliance.[[188]](#footnote-189) This potential negative impacts could be mitigated by promoting the appeal of the EU single market through e.g. trade measures. [[189]](#footnote-190)
* Companies switching to less risky suppliers or countries[[190]](#footnote-191) or shortening their value chain for better overview and traceability as a way to de-risk their value chain. This potential negative impact will be mitigated by requiring that the company ceasing, preventing and mitigating the harm should take into account the interests of the victims and affected stakeholders and help the value chain partner though sharing the burden, if necessary. Collaborative efforts will be fostered through support measures, etc. to ensure divestment for suppliers or countries stays the last resort[[191]](#footnote-192). Abandoning value chain partners may also be less likely due to difficulties to restructure value chains.
* Smaller and traditional businesses being pushed out of the market (disproportionate market barriers for smallholders) due to perceived lower level of control over them.[[192]](#footnote-193) Further to measures mentioned above, mitigation measures will include support measures, guidance on how to fulfil due diligence in smallholder models, as well due diligence fostering continuous engagement. For an overview of EU development cooperation actions accompanying EU regulatory and non-regulatory measures on sustainable supply chains, please refer to Annex 18.
* Companies under less stringent regulations in third countries (unless they generate a significant turnover at EU market and are thus subject to the same rules) seeking to leverage their position for a competitive advantage. [[193]](#footnote-194) Besides the coverage of third country companies, mitigation measures should foster the creation of a stronger regulatory environment in a host or third country and incentivize accountability of third country companies.
* Adverse perceptions (and possibly reactions) on third country side, as certain local practices express deep-rooted values and traditions[[194]](#footnote-195). Mitigation measures include country level cooperation, community outreach in third countries fostering stakeholder engagement which cultivates a willing workforce that shares the benefit and is empowered to take ownership and contribute to a just transition. [[195]](#footnote-196)

Accompanying measures can help foster the creation of a stronger regulatory environment in a host or third country thereby tackling the root causes of systemic issues in producing and manufacturing countries and ensure the sustainability transition is indeed just and beneficial to all supply chain actors[[196]](#footnote-197),[[197]](#footnote-198). Such accompanying measures are included in the list of EU development cooperation actions accompanying EU measures on sustainable supply chains in Annex 18.

### Consultation

In the feedback to the open public consultation, most respondents saw the positive effects of mandatory due diligence rules on third countries,

Respondents considered that with their economic commitment, their investments and their know-how, EU companies can contribute to sustainable growth and higher employment in developing and emerging countries. They highlighted evidence of targeted action on building trust and long-term relationships with a range of key stakeholders through engagement and due diligence processes leading to improvement in living and working as well as environmental conditions on the ground. They therefore stressed how adherence to proposed due diligence requirements would have strong positive impacts on workers in value chains as well as local communities in operating countries. Such positive impacts would drive progress towards the achievement of the UN Sustainable Development Goals.

A subset of respondents feared a potential negative impact of due diligence rules on third countries. More specifically, these respondents are worried about the fact that companies investing in third countries with weak or absent social, labour, and environmental rules, would have to withdraw their business from these countries if compliance with the due diligence rules is impossible. This could damage global trade and the jobs of many employees in developing and emerging countries. They therefore highlighted how it is important to, in parallel, have positive measures at local level in developing and emerging countries because 80% of workers are totally unaffected by global supply chains. In developing and emerging countries, the primary responsibility for compliance with human rights rests with the states and their governments. The international community must therefore not let up in its efforts to demand and enforce human rights in the local working environment. In that respect, strengthening international and multilateral cooperation, especially in the course of more intensive development cooperation, is also important.

Overall, similarly to the conclusion of the supporting due diligence study, also the public consultation respondents indicated that an European framework on more specific duty of care requiring companies to fully integrate sustainability risks and adverse impacts in corporate strategy and a mandatory due diligence duty would positively contribute to respect of human and labour rights not only within the EU but also in developing countries. This includes reduction in human trafficking, child labour and modern slavery, improved safety and working conditions of workforce throughout the global supply chains, improved health and standard of life of people around the world given the globalised supply chains.

## Social impacts

### Working conditions, employee satisfaction and health

#### Literature

The Supporting study on directors’ duties finds that with an **EU-wide formulation of directors' duties and company’s interest** enshrined in a new EU directive which require corporate directors to take into account **the interests of different company stakeholders**, and to identify and mitigate sustainability risks and impacts would result in more focus on the long-term, for the long-term benefit of all stakeholders. This is expected to result in an increased attention by the board to the social risks and impacts associated with company’s direct operations and in its value chain, eventually leading to adopting more sustainable and **long-term oriented policies on employees** (for instance increased investments in policies and programmes aimed at **workforce training**, **reward and retention**, investment into human and intellectual capital development, improving in this way the working condition of employees within companies). For employees, the impact might be particularly positive in those EU countries where board-level representation of workers is either absent or limited. Importantly, also stakeholders less able to influence the financial performance, but equally impacted by the company’s activities, such as the **local and global communities**, would receive higher attention. This might lead directors to identify and prevent negative impacts (e.g. on **health**) and promote positive impacts (such as **better wages**, other measures leading to better **employee satisfaction**), thus contributing to reducing social vulnerability and inequalities at macro level.

While also a human rights issue discussed hereunder, improving **occupational health and safety** conditions will be part of due diligence. As regards such impacts, the impact of the French law is too early to evaluate. However, for example, Section 1502 of the US Dodd-Frank Act (signed into law in 2010) requiring publicly traded companies to ensure that the raw materials they use to make their products are not tied to the conflict in Congo shows positive health and safety impact. The Enough Project conducted field research in 2015 and 2016 in Eastern Congo with miners, traders, human rights activists, civil society leaders, and foreign industry experts, to assess impacts of the legislation. The investigation found direct positive impacts including increased security for civilians in some mining areas and a significant reduction in armed group control in 3T mining areas. Additionally, a few indirect advances for rights-holders were found around improved safety and health standards for miners.

As regards **employee satisfaction**, a large business survey conducted by McKinsey in 2017 among 2,700 companies across different regions, company sizes and industries revealed employee satisfaction and attraction to be amongst the top reasons why companies address sustainability matters.[[198]](#footnote-199) The supporting study on due diligence found that CSR and sustainability activities can increase the attractiveness of a company for employees and improve employee satisfaction (Study on due diligence, p. 451). Furthermore, it found that about 2 in 3 respondents of a large online survey which covered 30 000 consumers prefers to work for a company that operates in a socially responsible manner (Study on due diligence, Annexure IV Table).

Employees are likely to stay with a company because of its CSR commitment, company image, culture and workplace itself (OECD, Table “summary of benefits of RBC in general p. 9). Employees report higher satisfaction levels when given the opportunity to have a direct social and environmental impact through their job.

Similarly, the meta-analysis by Clark et al[[199]](#footnote-200) assessing the relationship between sustainable management and a company’s economic performance found that good reputation regarding the working conditions can increase the company’s attractiveness for employers and can help to retain workers.[[200]](#footnote-201)

#### Consultation

In the feedback to the open public consultation on this initiative, when asked about the effects of due diligence rules, a high number of respondents stated that due diligence leads to “safer and more decent working conditions for supply chain workers including those in non-EU countries including health and safety, living wages and decent terms of employment.” They say that “in particular, due diligence would require companies to respond to sector specific risks such as heavy use of toxic chemicals or dangerous working sites and risks facing vulnerable groups, such as migrant workers, lower-caste workers, homeworkers, temporary workers, illiterate workers, children and women.”

Some respondents focus on the reduction of accidents at work in general and mention an improvement in safety and working conditions empowering workers in global supply chains. They also address the importance of companies being transparent about their working conditions, the structure of their value chains and the actions they undertake to uphold good labour standards.

Respondents listed employee satisfaction as one of EU level regulation direct benefits for companies. While seeing general improvements on health and safety of workers as a consequence of due diligence, some respondents listed healthy and safe working environment as one of the specific elements for which targets or minimum requirements should be set.

## Fundamental rights / human rights

### Literature

The supporting study on due diligence notes that the quantification of the effects on human rights are difficult to trace as they are often derived indirectly from changes in a company’s conduct as a result of reputational concerns (p. 325). In recent years, attempts have been made to develop auditing practices focused on human rights. Nevertheless, it has been acknowledged that such audits are fairly limited (p. 218) which indicates that – in spite of the growing awareness and commitments among businesses – risks to workers and the communities are yet to be managed adequately (p. 219). In fact, a 2018 study demonstrates that even when companies do look beyond their direct suppliers, audits that certify suppliers as compliant, even independent and high-quality ones, are not sufficient to ensure that an approach is credible and has any benefits for rights-holders[[201]](#footnote-202).

It is also important to note is that not only literature but also existing examples on impacts of due diligence regulation on human rights are scarce. The French Duty of Vigilance Law is often used as the primary example despite being too new to have already generated evidence-based insights regarding its impacts.

However, the survey of the Supporting study on due diligence clearly showed that the majority of respondents do not find the current legal landscape concerning due diligence requirements to be effective, efficient or coherent. (p. 94). A large majority of stakeholders considered that mandatory due diligence could have positive human rights impacts. Over 60% of respondents expect positive impacts on all human rights areas, and the top areas – with above 80% of responses – are the right to freedom from slavery, the rights of the child, women’s rights, the right to non-discrimination/equality, the rights of indigenous people, and the right to life, liberty and security of person. Additionally, most surveyed companies considered that new regulation requiring mandatory due diligence could have positive impacts on their supply chains. Over 60% of respondents expect positive impacts on 9 out of the 15 human rights areas, and the top areas – with above 70% of responses – are the right to freedom from slavery, the rights of the child, and women’s rights. (p.522). Interestingly, the survey also found that when looking from the perspective of economic sectors, there is a tendency to have positive prospects regarding the potential effects of mandatory due diligence among companies from the manufacturing sector, as well as among the retailing, agriculture and agribusiness, automotive and consumer goods sectors, while when it comes to company size, amongst SMEs, most companies have favourable prospects and amongst large enterprises, the great majority shares these prospects (p. 532).

Evidence from the 2015 assessment of impacts of the Dodd-Frank Act by the Enough Project shows that even when less than 100% of companies comply, mandatory due diligence requirements can have significant benefits. The investigation found direct positive impacts including increased security for civilians in some mining areas and a significant reduction in armed group control in 3T mining areas.[[202]](#footnote-203) In conclusion, the evidence of the efficacy of mandatory due diligence requirements seems to suggest that as long as robust risk assessment (based on those affected), transparency, monitoring, and compliance systems are enforced, rights-holders can expect opportunities for protection.

### Consultation

79.9% of respondents believes that an EU legal framework will lead to awareness of companies’ adverse human rights, social and environmental impacts and risks related to human rights violations other social issues and the environment and that it is in a better position to mitigate these risks and impacts.

Many respondents associate due diligence with “reductions in harassment, intimidation, threatening and killing of human rights, land and environmental defenders", describing due diligence as “fighting impunity at local and international level.” Other respondents talk more generally about improvements in the respect of human rights or solely focus on the role of due diligence in reducing cases of harassment and threats to trade union activists and human rights defenders.

Related to the stated benefits, many respondents believe that due diligence will lead to “reductions in land grabs and violation of the customary and other land rights of indigenous peoples and local communities in host countries, through recognition and respect for collective customary land rights collective and other legitimate tenure rights, including applying the principle of free prior and informed consent”. Some other respondents mention simply the improvement of indigenous peoples’ rights as a general benefit of due diligence rules. Three respondents point out that the prevention of conflicts with indigenous people can result in the avoidance of other disruptions and even more costs for companies.

As regards access to justice, the consultation focussed on both the litigation costs but also the benefits that potential victims have when a coherent EU framework is implemented. The consultation clearly shows that the due diligence duty would improve access to justice. Respondents highlighted the difficulties of victims to get access to remedy and the frequently faced obstacles (legal, procedural and practical) in attempting to hold European companies liable for the harm caused by their subsidiaries or supply chain partners located in a third country.[[203]](#footnote-204) Respondents believe that access to justice in the EU for rights-holders located in third countries should be facilitated through extended statute of limitations and through the application of the jurisprudential principle of equality of arms so business enterprises have an obligation to disclose all evidence in their possession related to the alleged violation.

## Environmental impacts

All of the identified possible impacts, i.e. fostering sustainable production and minimising environmental impacts, including with regard to climate change, biodiversity loss, degradation of ecosystems, pollution, efficient use of resources and circular economy will be discussed together, given that the very objective of the initiative is to drive companies towards sustainable behaviour in a broad sense, also including environmental aspects. The literature has demonstrated that the impact of environmental risks management and due diligence on environmental outcomes are positive. For a detailed overview of the literature one can look at the supporting study on due diligence tables 8.17 and 8.18.

Climate change [and possibly biodiversity, if the post 2029 Biodiversity agreement is adopted] are among the areas where the initiative will require setting a science based target, in case of climate change, it will be linked to climate neutrality by 2050 under the Paris Agreement for a certain group of companies.

Environmental **harm will be reduced as a direct impact of the initiative** in companies’ own operations and value chains. Due diligence will be linked to the respect of international agreements listed in the impact assessment report, i.e. those which contain specific duties that are implementable by companies, including the Paris agreements on climate change. As regards climate change, the requirement for certain companies to set science based targets as part of the corporate strategy will reinforce the impact of the due diligence duty by elevating this matter specifically to strategic level with concrete targets. The results of the OPC shows that a mandatory duty with target is expected by stakeholders, including businesses to lead to most benefit. In the EU, the impact will be the highest in sectors which are not yet subject to regulation. It will also have a positive impact in third countries as most climate impacts in some key sectors identified as high impact (for example manufacturing) is in the value chain located in third counties. As regards biodiversity, it is at this stage uncertain what the ambition of the post-2020 Convention will be in preventing biodiversity loss, so it is at this stage difficult to predict its impact. Because of the **interlinks between human rights and environmental harm** (for example an oil spill may also lead to preventing access to food or deposit of toxic waste may also generate illnesses) positive environmental impacts are also expected though indirect human rights impacts. The initiative is also likely to contribute to more efficient use of resources, improving the use of renewables in production processes, limiting the amount of waste produced, stimulate the clean disposal of waste (reduce toxicity).

Positive environmental impact will also arise from **preventing and minimizing environmental risks to the company**: the directors’ duty to manage sustainability risks will also reduce potential environmental damages such as emissions, leaks, break-downs, accidental emissions, fires, etc. including in the broader value chains. This positive impact will arise from the consideration that environmental risks, if materializing, can have significant financial repercussions on the company. For example, the impact assessment of the EU Climate Adaptation strategy states that with record high temperatures in 2020 globally and across much of Europe, and with a clear message from climate models that temperatures will continue to increase, the urgency to adapt seems undeniable. The IPCC Special report shows that even in a best-case scenario of sustained emission limitations, and global warming limited to 1.5°C, there will be severe stress on agri-food systems, ecosystems, natural capital, etc. Adapting to such stress in certain sectors would include investments which could have positive impact on the environment. Companies also depend on their natural environment, so they will have to avoid polluting it and invest into stopping environmental degradation etc. if they want to remain viable over a longer time horizon. For example, environmental degradation may have a direct impact on the quality of certain food and beverages products which depend on good quality ingredients, which will prompt avoiding pollution.

### Literature

Evidence shows that environmental due diligence already contributed to reduction of adverse impacts. For example, the EU Timber Regulation supported the upgrading of supply chain practices. Companies subject to the duties but also those in host countries invested in technology, monitoring and certification to drive improvements[[204]](#footnote-205).

The 2016 evaluation to the EU Timber Regulation indicates that the EUTR demonstrated itself to be highly relevant for tackling illegal logging and related trade by changing market behaviour patterns and freeing supply chains from illegally harvested timber. It is recognised as an important instrument to halt deforestation and forest degradation, enhance and maintain biodiversity, and address global climate change.

Evidence, including results of the EU Impact Assessment of Directive 2008/99/EC on the protection of the environment through criminal law[[205]](#footnote-206) demonstrates that harmonisation of due diligence requirements across national boundaries, as well as with existing regulatory tools, can be expected to provide positive environmental impacts through increased sanction levels, offence definitions, and scope of liability.

Increased certification and due diligence requirements have led to other supply chain development initiatives in third countries. Examples include farmer field schools which bring together a group of farmers, livestock herders or fisherfolk, to learn about how to shift towards more sustainable (including climate smart) production practices, by better understanding complex agro-ecosystems, agronomy and by enhancing business support services[[206]](#footnote-207).

Literature also confirms that areas with lax environmental regulation – i.e. pollution havens – strongly attract polluting firms and significantly explain the location choice of polluting affiliates[[207]](#footnote-208). This indicates that a horizontal due diligence duty applying to the entire value chain would discourage companies from taking advantage of pollution havens and would thereby contribute to protection of the environment.

### Consultation

The survey conducted for the Supporting Study on Due Diligence (Table 8.58: Specific impacts by environmental area) shows that the large majority of all stakeholders, including businesses expect positive environmental impacts. Considering economic sectors, there is a tendency to have positive prospects regarding the potential effects of mandatory due diligence among companies from the manufacturing sector, as well as among the retailing, agriculture and agribusiness, automotive and consumer goods sectors. More than half of large company respondents declare that it is likely that mandatory due diligence will have an impact on the environment. (p.540)

When asked about the content of a possible corporate due diligence duty in the open public consultation on this initiative, respondents that preferred minimum process and definitions approach with or without further requirements, indicated climate change mitigation (85.6%), natural capital, land degradation, ecosystem degradation, etc. (83%) amongst the areas to be covered in a possible due diligence obligation.In their answers, respondents highlighted that due diligence requirements should use relevant internationally recognized standards or guidelines.[[208]](#footnote-209)

Overall, respondents see environmental impacts as one of the benefits of action on sustainable corporate governance. More specifically, a frequently mentioned benefit is an improvement in the environmental impact of business operations such as the reduction of deforestation, use of pollutants and emission of greenhouse gases, more efficient use of resources, recycling of waste, reduction in the use of hazardous material etc. According to respondents, optimisation in this context should include “transition to cleaner forms of energy, more sustainable materials, circular economy models and responsible waste disposal”.

1. SME test

The specific impact of all policy measures on SMEs were screened ex ante for all options. The aim of the analysis was to check whether SMEs would be disproportionately affected and, where relevant, to include measures in the design of the policy options that would mitigate the burden on SMEs.

# Identification of affected businesses

This initiative is likely to affect a wide range of European companies, even if **all small undertakings and all medium-sized undertakings active in economic sectors where the risk of environmental or human rights harm is lower will be excluded from the scope of the due diligence rules** (except for listed SMEs in certain policy options other than the preferred one).

According to the calculations based on the indicative list of **high-impact sectors** in Annex 11, about **two-fifths of medium-sized companies operate** in such sectors and will therefore incur compliance costs in certain options (including the preferred option). In addition to direct costs, about **one fifth of medium-sized companies will indirectly incur costs** as they will be involved in the impact mapping and mitigation across the full range of possible adverse impacts as suppliers or subsidiaries of larger companies.[[209]](#footnote-210) This **trickle-down effect** is also to be expected with regard to **micro and other small companies**, as well as **SMEs of all sizes operating in a legal form other than limited liability companies (European and non-European)** that are **business partners or subsidiaries of larger companies under the scope** of the due diligence rules. However, **SMEs that are not active in sectors where the risk of human rights abuses or environmental harm is high, will be unlikely to incur significant costs** as a result of this initiative.

The trickle-down effect will likely materialise through **contractual clauses** included in B2B commercial contracts and **other measures** (such as joint development of action plans, investigations, change of production processes, etc.).

While large limited liability companies generate about three-quartersof the total turnover in the EU economy, the contribution of SMEs to the human rights and environmental harm along the value chains (including in non-EU countries) cannot be neglected as **many of them operate in sectors in which such adverse impacts are quite likely or where the combined impact of SMEs is even larger than those of large companies**.

Therefore, when designing the policy options and selecting the preferred one, account was taken, on one hand, of the need **to target those companies that enable the attainment of the initiative’s objectives without imposing a disproportionate burden on SMEs** and, on the other hand, of the need to **prevent a mere shift of obligations on to the regulated companies’ suppliers and other value chain partners**.

The options considered in this impact assessment use the **size** of limited liability companies (based on turnover, employee and/or balance sheet total data) as one of the criteria to identify the personal scope of the different obligations. An additional main factor is the **sector** in which the company carries out its main activity. Furthermore, various options were looked at to ease the burden on smaller companies by specifying **one or a limited number of adverse impact types** that a company should cover in its due diligence steps. Finally, a **phased-in application** for SMEs was included in all options, which will not only smooth out the initial costs of compliance but could possibly lower them further (due to possible joint industry initiatives being developed in the meantime, improved IT and other technology tools, etc.)

The initiative covers two other areas: directors’ duties and **remuneration**. The latter one will have **very limited impact in general, including on SMEs.**

The **directors’ duties** will **affect all or some limited liability SMEs directly**. The harmonised clarification of the **general duty** to act in the best interest of the company **is expected to influence corporate decision-making but will not result in immediate additional compliance cost**. From among the **specific duties implying additional costs** in addition to those borne under the due diligence obligation, the **science-based target setting was not considered to apply to SMEs** in any of the policy options assessed. To the contrary, the duty to **identify and manage sustainability (stakeholder-related) risks** was included in all policy options, however, with a personal scope limited to the directors of companies above a certain size and/or active in high-impact sectors. **No option covers small and lower-impact medium-sized companies** (except for those that have securities listed in the EU, in certain options). The **costs** estimated for the possible SMEs was estimated to **remain rather low**.

SMEs will also be **indirectly affected by the directors’ duties as they are stakeholders** of other SMEs or larger companies if they are the suppliers or customers thereof (direct or further down the chain). The employees of SMEs in the supply chain will also be stakeholders of the other companies concerned. This means that corporate decision-makers, including in larger companies, will have to **take into account the interest of their partner SMEs and the employees thereof** with a view to acting in the interest of the company, including in the longer run, which is expected to be beneficial also for the SME business partners of the company concerned.

# Consultation of SME stakeholders

While some respondents to the open public consultation see the benefit of a legal framework covering all EU companies, regardless of size, sector or type of incorporation to ensure the level playing field, different types of companies and business associations have called for a cautious, gradual and proportionate approach in order to take into account the impact on SMEs.

Out of the 855 non-campaign responses received in the open public consultation on this initiative, the business respondents were 191: **82 responses were received from SMEs** (33% from micro companies, 28% from small companies, and 39% from medium companies). Most SME respondents originate from Germany (26.83%) and Belgium (14.63%).

54% of SMEs expressing an opinion agreed that **corporate directors** should be required by law to **identify the company’s stakeholders and their interests**, and 63% agreed that they should **manage the risks for the company in relation to stakeholders** and their interests. Regarding the requirement that corporate directors should **identify the opportunities arising from promoting stakeholders’ interests**, 51% agreed while 49% disagreed with the need for a legal requirement that corporate directors should set up **adequate procedures and measurable (science-based) targets** to ensure that impacts on stakeholders are identified, prevented and addressed.

Regarding the need to clarify in legislation as part of directors’ duty of care that corporate directors should **balance the** **interests of all stakeholders** instead of focusing on the short-term financial interests of shareholders, 51% of the SMEs expressed support. 62% of SMEs expressed support for the need to **integrate sustainability risks, impacts and opportunities into a company’s strategy**, decisions and oversight within the company. 56% of SMEs disagreed with the proposition that **stakeholders should be given a role in the enforcement of directors’ duty of care**.

61% of SMEs preferred a **horizontal approach** as regards the content of a possible **corporate due diligence duty** over a sector specific or thematic approach. 26% of SME respondents preferred none of the listed options, 23% expressed preference for a **minimum process and definitions** approach complemented **with** **further requirements in particular for environmental** issues, while 22% chose a **minimum process and definitions approach**. The **principles-based approach** was chosen by 16% of SME respondents.

To **reduce the burden** linked to due diligence, SME respondents indicated that a toolbox/dedicated national helpdesk for companies to translate due diligence criteria into business practices would be most effective (44%), similarly to capacity building support including funding (41% ) and lighter reporting requirements for SMEs (40% ).

86% of SMEs agreed that due diligence rules should also apply to **third-country companies.**

Regarding an **enforcement mechanism accompanying a mandatory due diligence duty**, 60% of SMEs indicated that supervision by competent national authorities (administrative enforcement) with a mechanism of EU cooperation/coordination was the most suited option. 34% think that supervision by competent national authorities based on complaints about non-compliance with the obligation to set up and implement due diligence measures (and/or based on reporting, where relevant), with effective sanctions (for example fines) would be appropriate. Only 24% indicated judicial enforcement with liability and compensation in case of harm caused by not fulfilling the due diligence obligation as the most appropriate enforcement mechanism.

SMEs scored the **annual costs of compliance with binding law that requires impact mitigation aligned with science-based targets and a possible reorganisation of the supply chain the highest**, on a scale from 0 to 10: 8.0 (administrative costs), 7.4 (litigation costs) and 7.95 (other costs)). The costs linked to binding law requiring the setting up / improving of external impacts’ identification were estimated lower on the same scale: 6.0 (administrative costs), 5.5 (litigation costs) and 5.1 (other costs). The costs implied by a non-binding guidance was scored lowest: 2.6 (administrative costs), 1.9 (litigation costs) and 2.2 (other costs)).

Benefits are expected to be highest for the option of binding law requiring harm mitigation aligned with science-based targets and a possible reorganisation of the supply chain (average score of 6.1 on the scale of 0 to 10), followed by binding law with cost and benefits linked to setting up/improving external impacts’ identification costs (average score of 5.4) and non-binding guidance (average score of 3.8).

Some SME respondents saw benefits in the regulation applying to all companies because additional costs for individual companies would be limited and positive effects on the environment and climate could be higher. Stakeholders cautioning about overburdening small companies, even if regulation brings about competitive advantages and better profitability, suggested a “gradual transition that allows SMEs to slowly adapt”. They also saw an opportunity to reduce the burden for SMEs with additional capacity building support, including funding and the development of a toolbox or the setting up of dedicated national helpdesk for companies to translate due diligence criteria into business practices. In this regard, complementary support instruments from other policy areas would facilitate compliance with this initiative. For instance, EU development policy provides funding for improving responsible production practices in supply chains in third countries, while more direct support would be provided to the companies by broadening the Due Diligence Ready platform and providing SME support through Enterprise Europe Network.

# Literature on the impact of corporate due diligence on SMEs

The literature on the impact of due diligence regulations on SMEs can be summarised as follows[[210]](#footnote-211): 1) The relative administrative burden of SMEs (per unit cost of compliance) is generally greater than for larger companies (this is valid also for the ratio between compliance cost and turnover); 2) SMEs suffer from tighter contractual obligations imposed by their large corporate clients (see above the example from France); 3) SMEs may have less leverage to influence their suppliers, especially if their supply chain extends to foreign countries (for instance to extract the necessary information from their supply chain partners, to make them abandon certain practices, etc.) Given this, liability remains a serious concern for SMEs.[[211]](#footnote-212) Furthermore, SMEs tend to avoid litigation as much as possible and favour alternative dispute resolution mechanism, which are designed to be faster and less costly.

# Measurement of the impact on SMEs

The most likely and most significant cost implications of this initiative would be the **direct substantive compliance costs related to the due diligence obligation**. These include one-off (initial) and recurrent (annual) costs. For companies this would depend to a large extent on the size of their business and the sector of their economic activities, while other factors, including the complexity of their value chains, business model, the place of the company in the chain or the due diligence undertaken by others in the chain etc. also influence the costs encountered by the company. For instance, the costs would be relatively larger in the case of more business partners, longer and more complex value chains, in particular if located in third countries presenting higher risks, e.g. because of the generally lower labour standards and poorer working conditions.

Overall, the options have excluded upfront all micro companies from the scope, as well as non-listed small ones. This choice is due to proportionality considerations, because the vast majority of these companies have difficulties complying with due diligence obligations, even when those are not voluntary, because of high relative costs and lack of necessary skills or difficulty to reflect those costs in their prices.[[212]](#footnote-213)

For the other SMEs, options have kept their inclusion in the possible scope to the minimum, by restricting it to two groups, following risk-based considerations: **listed non-micro SMEs** (similar to the CSRD proposal) and **high-impact medium sized companies** (i.e. medium-sized companies operating in high impact sectors from a human rights or environmental point of view). This choice is considered to strike a balance between the capacity of those companies and the efficiency and effectiveness of this initiative.

For the first group, due diligence reporting would be covered by the CSRD review (in addition to taxonomy disclosures), which gives them 3 additional years for compliance and provides them with the possibility to report using a simplified reporting standard.

For the second group, due diligence reporting would be an additional obligation (as those companies are not in the scope of CSRD). Similarly to CSRD, a phasing in and the use of simplified reporting are foreseen. In addition, for all companies with less than 500 employees and 150 MEUR turnover/500 employees or 350 million turnover, due diligence will be limited to the most relevant risks for the high impact sector a company belongs to. This will allow those companies to focus their efforts where it matters the most.

For the companies covered by the scope of the policy options, the company size is one of the factors of correlation with the estimated compliance costs and we therefore estimated different average compliance costs for high-impact mediums-sized companies (also differentiating between listed and not listed to be able to calculate the additional costs compared to the dynamic baseline), large companies and the 300 largest EU companies. However, even within such size groups, companies can be very different in terms of complexity of the value chain, the sectoral differences, etc. and the estimated value has to be understood as average for the given company type (size, listed).

Many of the high-impact medium-sized companies are part of the value chains of larger companies and will most likely be already directly or indirectly impacted by the obligations of those companies that fall under the scope of the full due diligence obligation (large or very large companies, depending on the option). It is only for the purposes of cost calculations that the cost of targeted due diligence was used for these, in reality the additional costs will likely be lower and the large buyer company will also be required to limit passing over compliance burden to the SME value chain partner.

The impact assessment points to potential **cost savings** that may arise via various channels, such as:

* **Modern tracking and surveillance technologies and digitalisation** provide unprecedented solutions (for instance using drones, radars, smart sensors or distributed ledger), and can drastically reduce the cost of data gathering, on-site audits, monitoring and impact mitigation[[213]](#footnote-214). Furthermore, important cost savings could arise via **automation of contracts**[[214]](#footnote-215) (both B2B and B2C applications) and from a more systematic **use of important European digital data assets** (such as the Copernicus satellite data[[215]](#footnote-216) for the monitoring of such contracts, or Airbus Starling[[216]](#footnote-217) satellite data services to monitor sustainability objectives). **Artificial intelligence and machine-readable public disclosures** of other companies in the value chain which might also help make data collection and assessment more efficient.
* Total costs emerging in relation to the value chain would also be lower than the costs calculated for companies individually in case there are several EU companies sourcing from the same supplier. This is particularly relevant for SMEs as they often **purchase from the suppliers that are already under scrutiny** due to being part of the supply chain of other companies as well. The costs are expected to be lower for companies that rely on **suppliers which themselves carry out sustainability due diligence**. This is more likely if the supply chain is located in the EU or in a third country where social and environmental standards are high.
* **Industry initiatives** have also potential in **cost sharing** between companies that operate in the same sector or have the same supplier[[217]](#footnote-218). According to the study of the University of Sussex (2016)[[218]](#footnote-219) on cost and benefits of implementing due diligence policies, a quarter of the 29 companies surveyed estimated that **sectoral collaboration could reduce the costs by 25 to 50% and a further quarter by 50 to 75% of recurrent costs**. The more companies participate in industry initiatives, the higher the potential of cutting their costs. The Dutch evaluation[[219]](#footnote-220) of its national Responsible Business Conduct agreements finds an average cost per signatory of those agreements of EUR 85 000, which is due, on one hand, to high fixed implementation costs and, on the other hand, to the number of signatories of specific agreements: the agreement with the highest number of signatories registers the lowest cost per signatory, EUR 6 000. It also points to the need for a targeted approach by these RBC agreements to support SMEs.
* Additional cost reductions can be expected from **cross-sectoral cooperation**, for instance those aiming at scaling up the exploitation of the potentials in circular economy: innovations ensure that the waste of one sector is used as raw material by another sector, resulting in mutual benefits and improved compliance with due diligence obligations to reduce negative environmental impact[[220]](#footnote-221).

Still, the **SMEs that do not fall under the scope of any of the options considered for this initiative** will likely incur costs resulting indirectly from this initiative. The French experience shows that **80%** of French SMEs and midcaps (which are out the French law’s scope) are asked by their contractors on CSR issues, whether to sign a charter or a code of conduct, to declare themselves in conformity with the main social and environmental standards (health/safety, waste management, business ethics or human rights), to sign clauses in their contracts or to undergo an extra-financial evaluation[[221]](#footnote-222). It also shows supply chain companies, in particular SMEs, complaining about price pressure and lack of recognition of their (due diligence-related) efforts in prices. The exact costs will depend on various factors: number of supply chains of larger companies to which the SMEs is supplying, sector, position in the supply chain, prior experience with responsible conduct policies, etc.

**Estimating the indirect compliance costs** is a difficult exercise, especially considering the limits of the information collected[[222]](#footnote-223). Using the high-impact medium-sized company’s direct costs estimates (around EUR 24 200 for recurrent and 7 250 for one-off costs as most of them are not under the CSRD sustainability reporting rules and will be subject to a targeted due diligence only) would overestimate the costs even if this was used as an upper bound. Indirect costs will be **limited to the costs of certain due diligence activities** (e.g. data gathering, amending contracts with subcontractors, to some extent training and assessment of impacts). The costs of other due diligence activities (e.g. building and exercising leverage, collective engagement, public reporting) will **not arise** for them or will remain more modest. In addition, some parts of the costs that arise should be discounted as companies that fall under the scope of this initiative will have a **duty to support their suppliers**.

To minimize the likelihood of such indirect costs becoming excessively burdensome for SMEs (and de facto erasing the effect of exempting most SMEs from the due diligence obligations), **each option has elements to limit passing on excessive compliance burden to SME value chain partners**. In addition, in accordance with the directors’ duties to be clarified also in this initiative, business partners’ interests will have to be taken into account in directors’ decisions, including when discharging the due diligence obligation. If need be, it is considered whether the initiative could limit imposition of unjustified costs in contracts through identifying a list of elements that cannot be put into contracts to enforce the due diligence obligation, or establish model/standard contractual clauses (as done for instance for the [GDPR](https://ec.europa.eu/info/law/law-topic/data-protection/international-dimension-data-protection/standard-contractual-clauses-scc_en)).

# Assessment of alternative mechanisms and mitigating measures

Taking into account the principle of proportionality, concerns expressed by stakeholders, and technical feasibility, the measure has been modulated according to the severity and frequency of the risk SMEs / medium-sized companies will face in respective sectors. As explained above, specific measures may be considered to shield SMEs from increased administrative burden.

The preferred option considers the following elements for mitigating the burden on SMEs:

* As regards **due diligence:**
  + from the outset, small companies (below 50 employees) are excluded from the concept of high-impact SMEs;
  + the concept of high-impact medium-sized company allows to target the imposed obligations both in accordance with risk and with the resources available to the company;
  + to identify high-impact medium-sized LLCs, we propose three options in Annex 11;
  + due diligence obligations will first apply only to larger companies and will be phased in for high-impact medium-sized companies;
  + to further simplify reporting for high-impact medium-sized companies, non-listed SMEs will be subject to simplified reporting;
  + the scope of the enforcement by civil liability applies the same conditions as for larger companies but is limited only to most relevant impacts, defined by legislation, for high-impact medium-sized and midcap limited liability companies;
  + low-impact SMEs as well as high-impact micro and small companies would only be affected indirectly, but will be covered by supporting measures and a limitation to pass excessive burden on them.
* As regards **directors’ duties and remuneration**
  + The duties implementing the due diligence duty will be modulated according to the size of the company and will be deferred in time. Directors’ of low-impact SMEs will only have to comply with the harmonized general duty to act in the interest of the company, while directors of high-impact medium LLC would have an additional specific duty regarding risk management that would be phased in.

1. Legal Context in The Field of Company Law, Corporate Governance and Reporting of Sustainability-Related Information

Corporate governance frameworks traditionally aimed at ensuring that directors, considered to be the agents of the company owners (the shareholders), avoid decisions that serve their own interest instead of that of the company. Following the financial crisis, which revealed that institutional investors and asset managers behave as shareholders with a short-term focus, the main purpose of the EU corporate governance regulatory reform was to promote more long-termism in share ownership and shareholder engagement.[[223]](#footnote-224) To date, the directors’ duty to act in the interest of the company is regulated by national law.

The EU corporate governance framework combines legislative rules and soft law, in particular corporate governance codes.[[224]](#footnote-225) Corporate governance codes are voluntary “comply or explain” instruments applicable to companies listed on the highest segments of stock exchanges. They are adopted either by business associations, stock exchanges or other fora. Compliance is not mandatory, if the company deviates from the Code it has to give explanations to the market. Shareholders are expected to challenge companies in case of non-compliance by asking questions and voting in the general meeting. In some Member States compliance with the Code is subject to some monitoring by business associations or other bodies.

For several years, there has been a move towards regulating corporate governance as binding law due to the perceived limitations in achieving high corporate governance standards through “comply or explain” codes. The [**Shareholder Rights Directive (SRD)**](https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32007L0036) grants procedural shareholder rights; its amendment ([**SRD II**](https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32017L0828)) promotes long-term shareholder engagement and regulates, among others, remuneration policy and remuneration reporting regarding directors of listed companies. Good governance standards regarding directors’ remuneration were first promoted through Commission Recommendations[[225]](#footnote-226) to be incorporated in corporate governance codes. Due to the documented ineffectiveness of this approach in mainstreaming good practice[[226]](#footnote-227), such standards were introduced as binding in financial services legislation and in the SRD. Particularly, according to this, the remuneration policy should contribute to the business strategy, long-term interests and sustainability of the company and should not be linked entirely or mainly to short-term objectives. In addition, SRD II, which is complemented by the [**Commission Implementing Regulation (EU) 2018/1212**](https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32018R1212#:~:text=COMMISSION%20IMPLEMENTING%20REGULATION%20%28EU%29%202018%2F1212%20laying%20down%20minimum,exercise%20of%20shareholders%20rights%20%28Text%20with%20EEA%20relevance%29), also improved transparency of institutional investors and asset managers with regard to how they engage with the companies they invest in, and how they take into account and monitor the long-term and non-financial (ESG) performance of these companies and their environmental and social impact, requiring investors to disclose their engagement policy and their strategy.

In the aftermath of the 2007-9 financial crisis, the [**Capital Requirements Directive IV (CRD)**](https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A02013L0036-20210628)[[227]](#footnote-228) introduced corporate governance rules for credit institutions and systemic investment firms. From 2022, large financial institutions will also disclose information on environmental, social and governance risks, including physical risks and transition risks.[[228]](#footnote-229) The CRD includes remuneration rules that apply to material risk takers, including members of the management body and senior management.[[229]](#footnote-230)

The 2014 [**Non-Financial Reporting Directive (NFRD)**](https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32014L0095)[[230]](#footnote-231)imposed reporting requirements on sustainability-related matters for certain large companies across industry sectors with more than 500 employees. Those have to disclose environmental, social and human rights, corruption and bribery-related information (risk, policies, the outcome of those policies, key performance indicators and impacts). In case a company does not have a policy or procedure (e.g. for due diligence) in place, the report has to explain why this is the case (“comply or explain”). The recent [**Commission proposal for a Corporate Sustainability Reporting Directive (CSRD, revision of NFRD**](https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52021PC0189)**)** extends the scope of the companies covered[[231]](#footnote-232) and strengthens the standardisation of reported information. However, it does not impose material duties on companies other than public reporting requirements.

The [**Sustainable Finance Disclosure Regulation**](https://eur-lex.europa.eu/eli/reg/2019/2088/oj)[[232]](#footnote-233) governs how certain financial market participants should disclose sustainability information. Delegated acts are in the pipeline to require that sustainability should be part of the fiduciary duty of certain investors. The [**Taxonomy Regulation**](https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32020R0852)[[233]](#footnote-234) requires the Commission to set a classification of environmentally sustainable economic activities by defining technical screening criteria for each environmental objective. A first delegated act has recently been adopted [on sustainable activities for climate change adaptation and mitigation objectives](https://ec.europa.eu/info/publications/210421-sustainable-finance-communication_en#taxonomy), and a second delegated act for the remaining environmental objectives is planned for 2022.[[234]](#footnote-235)

Other important acts are the [**Transparency Directive**](https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A02013L0050-20131126)[[235]](#footnote-236) which requires issuers of listed securities to provide to investors financial information and information on major holdings, and the [**Takeover Bids Directive**](https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A02004L0025-20140702)[[236]](#footnote-237) that provides for common rules for takeover bids, in particular as regards the protection of minority shareholders in cases when control of a company changes hands, and the opportunity for employees of the companies concerned, or their representatives, to state their views on the foreseeable effects of the bid on employment.

1. Relevant EU legislation and policy initiatives

This annex describes the most relevant existing EU policies and upcoming EU policy initiatives that interact with the sustainable corporate governance initiative. It is divided into four parts: The following mapping table lists related EU policy measures and initiatives and illustrates added value of this initiative and synergies with the other related measures. Section 2 provides more details on the interaction with other existing or planned EU measures comprising supply chain due diligence obligations. Section 3 presents selected EU trade and developments cooperation support measures that can facilitate compliance with the due diligence obligation under this initiative.

# Mapping of interlinked existing and planned laws and added value of this initiative

| **Initiative / legislation** | **Obligations for companies resulting from the initiative/legislation** | **Which companies are covered** | **Possible synergies with the SCG initiative** | **Interaction with and added value of the Sustainable Corporate Governance initiative** |
| --- | --- | --- | --- | --- |
| **CSRD proposal (adopted on 21 April 2021, COM(2021) 189 final, 2021/0104 (COD))** | * **Disclosure** obligations as regards sustainability risks with a double materiality perspective, sustainability policies, measures, impacts, targets, due diligence processes, role of the board and management, how sustainability is integrated into the corporate strategy * **Mandatory audit** (limited assurance) of the reported sustainability information * Standardised and digital-ready reporting * The scope of companies that are subject to sustainability reporting requirements would be extended to **all large companies and all listed companies** with the exception of listed micro-undertakings. * **Voluntary simplified reporting for SMEs** to enable them to meet information demands from large company clients and banks and facilitate their contribution to and participation in the transition to a sustainable economy * Covers 1 out of 5 steps of the due diligence process | 49000 companies  Listed companies (not micros)  All large companies (according to the Accounting Dir Art. 3 definition)  SMEs: only listed small and medium in the scope.  The IA found a trickle-down effect on SMEs from NFRD in terms of requests for sustainability information. | Existing reporting requirements (NFRD) resulted in fostering good practices by frontrunners. About 45% of companies currently within the scope of the NFRD adopted some new due diligence processes on environmental or human rights matters because of the existing NFRD requirements.  Possible synergies: as collecting information for reporting purposes requires setting up some processes, the CSRD may help in the first step of the due diligence process, namely the identification of adverse impacts, including in the value chain. The CSRD will also cover the last step of the due diligence process, namely reporting, except for high- risk non-listed medium-sized companies. This initiative will lead to companies’ reporting being more complete and effective. Therefore, complementarity will increase effectiveness of both measures and drive true behavioural change. | * As the CSRD proposal relates to disclosure obligations, supervision concerns these only. * The CSRD proposal is not targeted at imposing direct obligation on the behaviour of companies (material duty, mitigation of risks and impacts), even though some behavioural effect may come indirectly. * Corporate liability for harm is not included.   Added value of the SCG initiative:   * Material duty for directors to take into account stakeholder interests and the long-term interest of the company, to manage risks to the company, integrate sustainability into the corporate strategy and duty for the company to mitigate external harm will lead to better corporate performance, integration of sustainability into corporate decisions and strategies, better risk management and less external harm; * Such duties also ensure that the reported information is reliable; * SCG and directors' duties have the potential to result in “integrated” corporate governance which may foster more integrated reporting and accounting where non-financial matters are duly reflected in financial analysis and corporate assets are priced taking into account the transition to a climate neutral and sustainable economy; * Supervision, liability for harm by failure to “prevent and mitigate impacts” is different from enforcement of a duty to “report” and will foster responsible business; * Scope covering also some third country companies allows ensuring a level playing field. |
| **Taxonomy Regulation** | **Disclosure**  The taxonomy is a classification tool aiming to help mobilize investments for achieving Green Deal objectives. The Taxonomy clarifies what constitutes an environmentally sustainable activity and thus, helps investors identify sustainable investments.  Art.8 of the Taxonomy Reg. requires to disclose information on how and to what extent economic activities of financial and non-financial undertakings are associated with environmentally sustainable economic activities, through three key performance indicators related to turnover, capital expenditure and operational expenditure.  In the draft DA, a **Capex plan** is also foreseen.  - it shall be approved by the management board of non-financial undertakings. Work is undergoing to identify harmful and neutral activities and to extend the taxonomy to social objectives (beyond social minimum safeguards) | Same scope as NFRD/CSRD (art 8 taxonomy regulation) | The taxonomy disclosures on the capex plan, where applicable, could help companies identifying capital expenditure/investment needs for the climate transition. | * Taxonomy provides a transparency tool that helps to facilitate investment decisions, tackle greenwashing as well as access to sustainability finance; * Its “substantial contribution to sustainability” criteria define the conditions for certain economic activities to be considered “dark green”. It does not define when an activity is “net zero”, but it is a flexible tool that allows to review SC criteria in time; * Value chain considerations are considered only partially in the taxonomy criteria.   Added value of the SCG initiative:   * SCG complements the taxonomy as it has the potential to further help investors to allocate capital to sustainable companies by requiring integration of stakeholder interests into directors decisions, proper management of sustainability risks and mitigation of impacts |
| **EU Initiatives/legislation comprising sectoral/supply chain due diligence,[[237]](#footnote-238) i.e.,**  **1) Conflict Minerals Regulation,**  **2) Batteries Regulation,**  **3) Deforestation initiative**  **(*see more detailed information below this table*)** | **Prevention, mitigation, reporting, monitoring**   * They apply to a very limited number of products (4 minerals in conflict minerals regulation, 6 agricultural products in the Deforestation initiative, 1 battery, etc.). * The due diligence requirement included in some of these sectorial initiatives aims at preventing some clearly identified risks (for example armed conflict and related serious human rights abuses in conflict minerals, deforestation risks only in the deforestation initiative); * They include a restriction to place products linked to deforestation on the EU market; * The Deforestation initiative also includes a legality requirement to ensure that illegal timber is not placed on the market. | Companies of all sizes are covered, but scope may be restricted through the use of thresholds applied to the quantity of imported product | Where the company covered by these instruments carries out other economic activities where the SCG will be applicable, it will benefit from due diligence processes imposed by the sectorial rule for identifying other types of harms as well in its value chains. | * These product-related/sector-specific initiatives are targeted to specific economic activities; * Having a risk-based approach, they cover specific sustainability risks, e.g. the Deforestation initiative only covers environmental risks associated with deforestation (except for the batteries regulation as regards risks); * They do not contain a liability regime for harm caused.   Added value of the SCG initiative:   * A horizontal due diligence duty covers all economic activities for all human rights, climate, environmental adverse impacts. * Horizontal due diligence would complement as *lex generalis* these initiatives as regards activities or risks that are not covered in the sectorial initiative, for example deforestation in construction, mining, etc. or environmental risks related to mining of conflict minerals would be covered by the horizontal due diligence. * Liability for harm could be an additional driver for effective implementation; * SCG aims to foster better engagement with suppliers and improvement of sustainability standards at production sites in third countries. |
| **EU legislation imposing accountability for environmental harm within the EU**  Environmental Liability Directive (ELD) | **Prevention and mitigation**  -ELD requires preventive and remedial actions if there is an imminent threat of damage occurring or damage occurred  -The company must pay for preventive actions and remedial actions (“polluter pays”)  -Environmental damage (land, water) is limited to some sectors (energy, metals, minerals, chemical, waste, large-scale pulp, paper, and food production) or to damaging of protected species and natural habitats | For some sectors only large-scale installations are covered and only the direct operator of the installation has obligations | The systems set up to ensure prevention of imminent threat to the environment within the EU may partially help fulfilling the due diligence duty for own operations in the sectors where the ELD applies. SCG might also partially solve certain problems identified with the ELD implementation and enhance liability when environmental harms occur. | The ELD   * Applies only to some sectors; * Applies only to harm to land, water and protected species; * Applies to own operations only, does not apply to the value chain; * Prevention only if there is imminent threat of damage; * Does not include civil liability, the ELD does not give private parties a right of compensation as a consequence of environmental damage or of an imminent threat of such damage occurring.   Added value of the SCG initiative:   * Horizontal due diligence duty complements the ELD as regards own operations by covering all sectors and applying to all environmental harms; * It will apply also to the value chain; * “ELD liability” is different from civil liability, it aims to ensure that the operator is financially liable to restore the state of the environment. Civil liability accompanying horizontal due diligence gives a right for private parties to go directly to court, ask for compensation for the harm suffered |
| **Other EU environmental legislation** | - Various other environmental laws introduce absolute limitations for companies on the release of some pollutants, etc. define EU goals (climate law) or set targets (for energy efficiency), define obligations for Member States (for example on protection of natural habitats), etc.  -The EU Eco-Management and Audit Scheme (EMAS) is a **voluntary** “management instrument” for companies to “**evaluate, report, and improve** their environmental performance”. It requires companies to **perform an environmental review.** It covers issues such as climate, air quality, water quality, natural resources availability and biodiversity, as well as cultural, social and political circumstances. |  | Voluntary EMAS systems set up by companies could help fulfilling the due diligence duty where they exist if adapted to the new requirements. | Other environmental legislation   * does not apply to the value chain, where 80-90% of the environmental harm occurs; * is rarely phrased in terms of corporate due diligence requirements and therefore does not include an obligation to set up systems to assess, prevent and mitigate the impact in EU or third countries. Existing soft law standards such as the EMAS provide interesting examples of how due diligence requirements are applied, albeit currently on a voluntary basis; * does not include civil liability.   Added value of the SCG initiative:   * Directors' duties ensure that the interest of the environment is taken into account in all directors' decisions and sustainability matters are integrated into corporate strategies; * SCG implements higher ambition of the European Green Deal; * Due diligence would become mandatory and apply also within the EU; * Horizontal due diligence extends compliance with international environmental agreements to the value chain where most harm occurs; * Civil liability ensures effective implementation and gives right to remedy; * Scope covering some also third country companies creates a level playing field.   An environmental law expert in the due diligence study summarises the added value as follows: “*although there is currently a “bricolage” of legal instruments aimed at the protection of the environment, the French Duty of Vigilance Law is currently the “the first legislative model worldwide that places the burden of responsibility of prevention on the multinational company, which incurs its civil liability for its activities and environmental externalities...”.* |
| **Climate legislation, “fit for 55” , biodiversity** | The revision of the **Emissions Trading System** (ETS). Today, the system captures and caps approximately 40% of the European Union’s greenhouse gases emitted from the power sector, large industrial installations and aviation within the European Economic Area. The revision strengthens the contribution of the ETS to the more ambitious emission reduction target of at least -55%, aligning also the cap on emissions with the higher climate ambition, tighten the regime for aviation and extend the system to emissions from maritime transport, as well as introduce emissions trading to emissions from road transport and buildings.  The **Carbon Border Alignment Mechanism** (CBAM) will aim at ensuring that products that are subject to a carbon price in the ETS when they are produced in the EU are subject to a similar carbon price when they are imported in the EU.  The revision of the **CO2 emission standards for new cars and vans** aiming at accelerating the supply to the market of zero-emission vehicles. The legislation would be strengthened in order to ensure a clear and realistic pathway towards zero emission mobility  Other rules on energy efficiency targets, renewable energy targets, effort sharing regulation do not directly apply to companies. | ETS covers only most emitting sites in the covered sectors | EU targets may help companies identify the corporate climate neutrality target and assess the magnitude of climate change risks resulting from the transition.  The CBAM complements this initiative:  The objective of CBAM is to incentivise decarbonisation of products imported in the EU. CBAM would therefore be an additional incentive for businesses concerned to become climate-neutral in their supply chains outside the EU. | * Revised ETS will not cover all sectors horizontally, it will not apply to some key sectors, such as agriculture, manufacture of food, textiles, pharma, IT, services, etc.) and does not capture so called scope 3 emissions (i.e. emissions in the value chain) which may represent up to 90 % of the emissions of the company. * The Carbon Border Alignment Mechanism (CBAM) will cover few sectors/products the import of which will be subject to payment at the EU border.   Added value of the SCG initiative:  - The “fit for 55 package” will focus on contributing to the delivery on the reduction of CO2 emissions within the EU. The SCG contributes significantly to an all economy transition, including in the value chains where the biggest impacts are, with proper sanctions and liability when harm is caused. SCG is also important to allow financial market investors to allocate funds efficiently in the market.  -EU and national targets exist in some areas (climate change, renewable energy or energy efficiency, biodiversity, etc.), they are high level and they need to be translated into individual corporate targets and, in turn, corporate action. Moving from EU-wide targets to corporate level action is urgent given how pressing a rapid and deep transformation of the economy is if we are to reach our targets.  -Furthermore, as regards climate change for example, energy efficiency and use of renewable energy actions (as announced as key elements of the fit for 55 package) will not, by themselves lead to climate neutrality. Transformation of production processes (circularity, process efficiency, fuel-switching, etc.) and technological progress will be necessary to achieve it. Individual targets will take the impact of such transformations also into account. Furthermore, SCG is complementary to existing and planned EU climate action including carbon pricing and national targets. |
| **EU health and safety and human rights legislation**  **(GDPR, Seveso, OSH Directives,** **Pay Transparency Proposal, etc.)** | -The Seveso III Directive requires industrial establishments, where dangerous substances are used or stored in large quantities, to put in place safety measures to prevent major accidents in industrial installations.  -The General Data Protection Regulation (“GDPR”) requires the exercise of due diligence with regard to one specific human rights impact: the right to privacy. The GDPR applies to the processing of personal data by EU-based companies, regardless of whether the processing takes place in the EU, as well as to the processing of personal data of data subjects who are in the EU by a non-EU company, where the processing activities are related to goods or services offered in the EU.  - The Pay **Transparency** proposal requires companies with at least 250 employees to have pay structures and transparency measures in place ensuring that women and men are paid equally for the same work or for work of equal value. | Companies of all sizes  The Pay Transparency proposal would apply to all employment relationships governed by a Member State's law. | Possible synergies for the due diligence process: the systems set up to ensure prevention of health and safety, privacy, etc. in regulated areas and sectors may help with due diligence duty in own operations. | EU health and safety and human rights legislation   * covers very specific risks (privacy, health aspects related to dangerous substances) * no civil liability * do not apply to the value chain   Added value of the SCG initiative:   * Horizontal due diligence to apply to all human rights harm in own operations and in the value chain across all sectors and outside the EU; * SCG will include a civil liability regime; * Scope covering some also third country companies, creates a level playing field. |
| **Sustainable product initiative (*see more detailed information below this table*)** | It aims to make products fit for a climate-neutral, resource-efficient and circular economy   * will create a framework for setting performance and information requirements on specific product groups in relation to range of environmental impacts and product aspects; * SPI requirements are conditions that have to be fulfilled in order to place a product on the market; * may include requirements on life cycle environmental impacts (e.g. on carbon footprint); * requirements to be set as relevant to specific products based on dedicated preparatory studies, going product-per-product based on pre-set priority criteria * may include information requirements related to social indicators;   Likely disclosure of sustainability information via digital product passport | All companies placing on the market products covered by SPI measures | Possible due diligence measures relating to specific social or human rights risks and to specific materials or processes may be adopted via SPI delegated act as regards certain specific product groups if dedicated preparatory studies confirm the need for such rules, taking into account the impact of the sustainable corporate governance initiative.  No civil liability. Possibility to restrict the placing on the market of products stemming from economic operators not complying with SPI due diligence requirements. | - All sectors and all sustainability factors will be covered under SCG, whereas SPI due diligence requirements would only focus on specific social or human rights risks identified in relation to specific products.  - SCG will be *lex generalis* compared to SPI which is *lex specialis*. |
| **Competition Policy – Revision of the two Block Exemption Regulations for horizontal cooperation**  **agreements and the Horizontal Guidelines** | The revised Horizontal Guidelines guidance would assist companies in self-assessing, horizontal cooperation agreements that pursue sustainability goals. | Companies of all sizes | Considerable synergies, as revised Horizontal Guidelines could facilitate industry cooperation in due diligence matters and thus potentially make due diligence more effective, efficient and lead to cost-sharing opportunities. | n/a |
| **Trade measures: - - Trade Policy Review,**  **Generalised System of Preferences (GSP),**  **TSDs** | The new GSP regime (GSP+) will enhance the conditionality on human rights and environmental issues for both environmental and human rights abuses by:   * Including additional international instruments on human and labour rights in the list of relevant conventions; * Adding the export of goods made by internationally prohibited child labour as a ground of withdrawal of preferences; * Including an urgent procedure for temporary withdrawal of preferences for exceptionally grave violations, where a rapid response is needed.   The Proposal also extends the obligations related to ‘negative conditionality’ to the relevant international conventions on climate/environment and good governance, and adds the Paris Agreement on Climate Change to the list of relevant conventions. |  | Trade policy measures can complement the SCG initiative and lead to synergies as they share the objective of making EU trade and supply chains more sustainable. | The effective application of mandatory human rights and environmental due diligence under SCGI - in particular throughout EU supply chains in GSP beneficiaries - would be supported by an updated GSP scheme to the extent that it is based on the same international conventions on human and labour rights, climate and environmental protection and good governance. |
| [**Directive**](http://ec.europa.eu/newsroom/just/item-detail.cfm?item_id=620400) **on the protection of persons reporting on breaches of Union law** | Protection for whistle-blowers who report breaches of EU law.  It establishes safe channels for reporting both within an organisation and to public authorities.  The Directive covers the fields of public procurement; financial services, money laundering and terrorist financing; product safety; transport safety; environmental protection; nuclear safety; food and feed safety, animal health and welfare; public health; consumer protection; privacy, data protection and security of network and information systems. It also applies to breaches of EU competition rules, violations and abuse of corporate tax rules and damage to the EU's financial interests. |  | This directive can complementary to SCG on the enforcement element of the due diligence requirements |  |
| **Summary of what systems based on existing EU law or voluntary measure could help in fulfilling the due diligence obligation including in the value chain:**   * Risk and impact identification systems set up as a follow up to the CSRD could help fulfilling step 1 of the due diligence process (identification); * EU environmental and human rights legislation facilitates compliance with the due diligence duty in companies’ own operations/ in the EU. * Voluntary EMAS systems set up by companies (so far limited) could help with fulfilling the due diligence duty where they exist, if they are adapted to the new requirements; * The GSP+ scheme would support the due diligence duty to the extent that it is based on the same international conventions on human and labour rights, climate and environmental protection and good governance. | | | | |

# Additional information on existing and forthcoming EU measures comprising sectoral due diligence obligations

This section describes more in detail existing and forthcoming EU measures comprising due diligence obligations that interact with this initiative:

* Conflict Minerals Regulation
* Proposal for a revised Batteries Regulation
* Deforestation initiative
* Sustainable Product initiative

## Conflict Minerals Regulation

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| **Title** | **Regulation (EU) 2017/821 laying down 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** |
| **Legislative or non-legislative** | Legislative – entered into force in January 2021 |
| **Description of policy or legislation** | The Regulation aims to:   * ensure that EU importers of 3TG (tin, tungsten, tantalum and gold) meet international responsible sourcing standards, set by the Organisation for Economic Co-operation and Development (OECD); * ensure that global and EU smelters and refiners of 3TG source responsibly; * help break the link between conflict and the illegal exploitation of minerals; and * help put an end to the exploitation and abuse of local communities, including mine workers, and support local development.   The Regulation will directly apply to companies that import tin, tungsten, tantalum and gold minerals and metals into the EU, no matter where they originate.  The Regulation requires EU companies in the supply chain to ensure they import these minerals and metals from responsible and conflict-free sources only.  EU importers of tin, tantalum, tungsten and gold must check what they are buying, to ensure it has not been produced in a way that funds conflict or other related illegal practices.  The regulation requires importers to follow a five-step framework in accordance with the 'Due Diligence Guidance for Responsible Supply Chains from Conflict-Affected and High-Risk Areas' (OECD Guidance).  These steps require an importer to:   * establish strong company management systems; * identify and assess risk in the supply chain; * design and implement a strategy to respond to identified risks; * carry out an independent third-party audit of supply chain due diligence; and * report annually on supply chain due diligence. |
| **Interaction with sustainable corporate governance** | The Conflict Minerals Regulationis a product specific regime and will put in place more specific requirements for conducting due diligence for certain products, thus it is *lex specialis* compared to the SCG initiative regarding the products covered by the Regulation. |

## Batteries Regulation

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| **Title** | **Proposal for a Regulation concerning batteries and waste batteries, repealing Directive 2006/66/EC and amending Regulation (EU) No 2019/1020** |
| **Legislative or non-legislative** | Legislative – forthcoming – Commission proposal of 10 December 2020 (COM(2020)798) |
| **Description of policy or legislation** | The initiative aims at modernising the EU's legislative framework for batteries. It is an integral part of the EU's Green Deal.  The proposal establishes requirements on sustainability, safety, labelling and information to allow the placing on the market or putting into service of batteries, and requirements for the collection, treatment, and recycling of waste batteries. The product requirements are tailored according to the type of batteries (portable, automotive, electric vehicle, industrial batteries) and the sustainability requirements concern the whole life cycle of batteries, including restrictions on hazardous substances, labelling and maximum level of carbon footprint over the life cycle, minimum content of certain recycled metals, performance and durability, and removability and replaceability.  It contains a requirement for the economic operators that place electric vehicle and industrial batteries on the EU market to establish supply chain due diligence policies regarding the sourcing of cobalt, natural graphite, lithium and nickel, and chemical compounds based on these necessary for the manufacturing of the active materials of batteries. |
| **Interaction with sustainable corporate governance** | The proposal includes due diligence requirements, which the sustainable corporate governance initiative also considers.  The two regimes would be complementary, whereby the Batteries proposal would be *lex specialis*, because the due diligence requirements for batteries are more specific than the horizontal duty in the context of the sustainable corporate governance initiative:   * They apply to **economic operators (manufacturers, importers) placing electric vehicle batteries (including incorporated in vehicles) and industrial batteries larger than 2 kWh** on the EU market, estimated to be **about 50** economic operators. * They concern **only those raw materials for which use in batteries is or is projected to be a significant share of the global use of those raw materials** (cobalt, natural graphite, lithium, and nickel), covering the entire supply chain. Compliance verification is in line with the general framework for EU requirements on (non-food) products (as also for the other requirements in the proposal); * The economic operators concerned must submit compliance documentation for third party verification by notified bodies, and they are subject to checks by national market surveillance authorities.   Recital 70 of the proposal lays out its interaction with legislative instruments containing supply chain due diligence obligations. It stipulates that “[o]*ther EU legislative instruments that lay down requirements regarding supply chain due diligence should apply in so far as there are no specific provisions with the same objective, nature and effect in this Regulation which may be adapted in the light of future legislative amendments*”. |

## Deforestation and forest degradation proposal

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| **Title** | **Proposal for a Regulation concerning certain commodities and products associated with deforestation and forest degradation** |
| **Legislative or non-legislative** | Legislative – forthcoming – proposal scheduled for the end of 20221 |

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| **Comparison of due diligence systems** | | | |
| **Issue** | **Sustainable Corporate Governance** | **Deforestation** | **Comments on interplay** |
| **Duty holders** | Large limited liability companies (500 employees+ or turnover +350 million / 500 employees and turnover EUR 150m+) + high-impact medium-sized and large companies  Third country companies with significant turnover at EU market | Operators, defined as businesses placing products in scope for the first time on the EU market (irrespective of size)  Large traders | It is expected that a large proportion of operators as defined in the deforestation initiative would also be covered by the due diligence obligation under the SCG initiative, including medium-sized companies. This is because the commodities covered by the deforestation initiative would likely be included in the list of high-impact sectors under the SCG initiative (e.g. agriculture, manufacture of wood, manufacture and wholesale of food products). |
| **Yardstick** | Relevant sustainability targets adopted by each company as part of the corporate strategy, including science-based targets as regards the GHG emissions mitigation and [biodiversity]; international environmental agreements, human rights conventions | EU-wide deforestation-free definition included in the legislation and obligation to ensure negligible risk of deforestation in products in scope placed on the EU market | Deforestation targets for relevant companies under SCG would necessarily need to integrate the obligation in the deforestation regulation as it will be legally binding |
| **Establishment of due diligence system** | Establishing a strong management system/process and engaging with stakeholders on due diligence.  The SCG due diligence obligation will cover companies’ own operations and value chain. | Each operator to take the appropriate measures to establish the due diligence system and the necessary processes.  Large traders are subject to the same due diligence obligations as operators | Equivalent in both initiatives.  Specific requirement for stakeholder involvement in the SCG initiative. |
| **Due diligence: information gathering** | Gathering and maintenance of relevant information necessary for the next steps, including mapping of the value chain | Gathering and maintenance of relevant information necessary for the next steps | Equivalent process although SCG initiative requires gathering information about additional impacts given its broader scope |
| **Due diligence: risk assessment** | Identifying and assessing actual and potential adverse impacts and risks | Analyse and evaluate the risk of deforestation in the supply chain - from harvest, processing and/or production. | Similar type of process |
| **Due diligence: risk mitigation measures** | Acting upon the findings, i.e. preventing risks of adverse impacts and mitigating actual adverse impacts in own operations and the value chain. This may entail need for prioritisation. | Where risk identified is non-negligible, take adequate and proportionate measures in order to effectively minimise the risk of not meeting the deforestation-free requirement | Similar process, but measures may be different given the scope and the underlying legal obligations. The prohibition to place products on the EU market associated with deforestation is a legally binding obligation that needs to be met from the date of application of the Regulation. This means it drives businesses away from unsustainable practices in the supply chains and promote changing to sustainable suppliers. SCG targets behavioural change, the SCG aim is rather engaging with existing suppliers to improve conditions, divestment of changing supplier being the last resort. |
| **Due diligence: tracking effectiveness and review** | Tracking the effectiveness of these actions. This may imply creation of operational-level grievance mechanisms. | Regular update of information and review of suppliers including risk assessment | Similar feedback mechanisms are expected where the due diligence system is kept under review, being an ongoing obligation. |
| **Due diligence: disclosure obligations** | Communicating how adverse impacts are addressed (this relates to reporting obligations which will be covered by the CSRD to a certain extent, i.e. within its scope). | Large operators and traders should publicly report as widely as possible, including on the internet, on their due diligence system including on the steps taken by them to implement their obligations | For deforestation, disclosure obligations should rely on the CSRD |
| **How is the burden related to low risk business operations and supply chains handled?** | Low risk SMEs are excluded from the scope | Through reduced due diligence obligations for products originating from low risk countries, as established through a Commission led benchmarking exercise.  Reduced level of inspections from competent authorities is also expected. | Different approach given the different framework of the initiatives but achieving similar objectives in terms of reduced costs for businesses that engage in low risk operations or value chains. |

## Sustainable product initiative

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| **Title** | **Sustainable product initiative** |
| **Legislative or non-legislative** | Legislative – forthcoming – proposal scheduled for the Q1 of 2022 |
| **Description of policy or legislation** | The Sustainable Product Initiative (SPI) responds to the objectives of the Green Deal and the new Circular Economy Action Plan.  This initiative will aim to make products fit for a climate neutral, resource efficient and circular economy, reduce waste and ensure that the performance of frontrunners in sustainability progressively becomes the norm. The focus is on requirements for the placing of products on the EU market. This should include specific design requirements (for example on resource efficiency, durability, reparability, recycled content), information requirements (presence of hazardous substances, etc.) and it may include social aspects where relevant and feasible.  As a legislative proposal, SPI intends to widen the scope of the Ecodesign Directive beyond energy-related products so as to make it applicable to the broadest possible range of products and make it deliver on circularity.  Measures adopted under SPI can include supply chain due diligence requirements with respect to social/human rights’ concerns related to specific products. |

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| **Comparison of due diligence systems** | | | | |
| **Issue** | **Sustainable Corporate Governance** | **Sustainable Product Initiative** | **Comments on interplay** |

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| --- | --- | --- | --- |
| **Description of due diligence duty** | Horizontal duty applicable to all sectors and to the entire value chain:  1. Identify actual or potential adverse human rights and environmental impacts in own operations and in the value chain;  2. Prevent risk of and mitigate adverse impact in own operations and in the value chain;  Mitigating measures include, as appropriate:  - joint development of corrective actions with the supplier,  - joining forces with other companies to exert influence on the supplier;  3. Track the effectiveness of measures;  4. Establish internal complaint mechanism;  5. Report on due diligence activities - covered by the Corporate Sustainability Reporting Directive. | Set due diligence requirements in relation to specific social or human rights risks associated with specific materials, components or production processes relevant to the product covered by an SPI measure. This empowerment is intended to be used where the relevant preparatory study identifies such specific risks and finds that other legislative instruments, including the SCGI, do not sufficiently address them.  In the process of developing due diligence requirements, care will be taken to ensure consistency/complementarity with the SCGI’s general requirements on due diligence.  The aim is to progressively ensure that products available on the EU market are not linked to certain social or human rights violations - identified on a product-per-product basis as most relevant for products’ individual supply chains. | Under SPI, additional or more specific due diligence obligations could relate to specific parts of the supply chain (e.g. more stringent requirements regarding the sourcing of a particular raw material). SPI could also require that, for specific risks related to specific products, due diligence obligations could apply to all economic operators placing those products on the EU market – regardless of company size.  SPI information requirements may also facilitate compliance with SCG requirements by generating information about the impacts related to products’ value chains. |
| **Impacts covered** | Human rights (including labour rights as set out in the ILO core conventions) and the environment (including climate change, biodiversity, pollution, etc.) | Environmental impacts will be covered by performance or information requirements, while due diligence requirements will focus on social and human rights risks linked to the supply chain of specific products. |  |
| **Product groups** | All industry sectors are in principle covered, at least as regards the largest companies. | All products with the exclusion of food and feed. Priority product groups: are likely to be those identified by the Circular Economy Action Plan (CEAP), e.g. textiles and furniture.  SPI will be implemented by implementing measures setting requirements for specific products or groups of products, going from product to product based on priority criteria. |  |
| **Instrument** | New | Revamped Ecodesign (legal instrument to be decided) and implementing measures adopted under it. |  |
| **Scope** | Companies based in the EU and companies generating a significant turnover in the EU, based on size.. | No link to size of company. SPI due diligence obligation would a priori apply to all economic operators placing on the market specific products in the scope of relevant SPI measures. | There are likely to be companies that given their size or involvement in a specific sector are covered by the SCG and that are also covered by due diligence requirements under the SPI because they place on the EU market products covered by an SPI measure including such requirements. SPI will take fully into account SCG due diligence steps and sectoral guidance to ensure coherence and to allow companies covered by both initiative to integrate their SPI due diligence obligations into their due diligence system set up pursuant to SCG. |
| **Enforce-ment** | Likely a combination of civil liability and administrative enforcement | Possibly third-party verification of compliance, recall or withdrawal of products. |  |
| **Third country coverage** | Companies generating a significant turnover in the EU | All third country economic operators placing products on the EU market | SPI would cover certain companies that are not in the scope of SCG.  It has a product focus and application is triggered by placing a product on the market. |
| **Interlinkage** | The SCG due diligence is *lex generalis* and would apply “*in so far as there are no specific provisions with the same objective, nature and effect*” in the SPI instrument, see also Recital 70 of the Batteries Proposal.  Where the SCG due diligence regime contains more specific provisions or adds requirements to the SPI, such provisions should be applied in conjunction with those of the SPI. | Like other EU product-specific legal instruments containing a due diligence duty, the SPI due diligence regime would *be lex specialis*. | SPI due diligence obligations will be based, to the extent possible, on the rules and concepts included in the SCG. Consistency and complementarity will be ensured at product-specific level to allow companies within the scope of SCG that also place products on the market subject to SPI due diligence obligations to comply with both sets of rules and minimise administrative burden. When deciding about the need for specific product-focused due diligence requirements, the interest of not creating a proliferation of unnecessarily different regimes will be duly considered. Depending on the product and risks at hand, SPI due diligence would focus on specific steps and add more detailed instruction as appropriate. |

## Sustainable food systems

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| **Title** | **Framework legislation for sustainable food systems (FSFS)** |
| **Legislative or non-legislative** | Legislative – forthcoming - proposal scheduled for the end of 2023 |
| **Description of policy or legislation** | The Farm to Fork Strategy Communication announced a legislative proposal for a sustainable food system framework. The aim is to promote policy coherence at EU and national level, mainstream sustainability in all food-related policies and strengthen the resilience of food systems. The establishment of common definitions, general principles and requirements for sustainable food systems and foods, responsibilities of all actors in the food system are some of the building blocks that will be considered as part of this initiative. Combined with labelling on sustainability performance of food products and with targeted incentives, the framework will allow operators to benefit from sustainable practices and progressively raise sustainability standards so as to become the norm for all food products placed on the EU market. |
| **Interaction with sustainable corporate governance** | The following links can be identified:  The work on the FSFS is ongoing and it is not possible at this stage to foresee the outcome of the Impact Assessment and the content of the possible legislative proposal. However a legislative initiative of this nature (framework legislation) is expected to look into definitions, including the definition of sustainability of the food system and the responsibilities of food systems actors. It will be important to ensure consistency on terminology and obligations throughout the different Commission initiatives linked to sustainability. |

## Code of Conduct for sustainable business and marketing practices

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| **Title** | **Code of Conduct for sustainable business and marketing practices** |
| **Legislative or non-legislative** | Non-legislative (voluntary commitments) |
| **Description of policy or legislation** | Voluntary commitments by the “middle actors of the food chain” i.e. food businesses, retail, hospitality and food service sector. However also other actors such as primary producers, input industry, packaging industry etc. have pledged.  In general terms, the aim of the Code is to encourage food business actors to voluntarily, but tangibly, improve their sustainability performance, while ensuring economic viability and resilience. The Code should allow adherence by a broad range of operators, including SMEs (within the limits of their size and capacity).  This is the main action under the Farm to Fork Strategy aimed at improving the sustainability performance of business operators primarily ‘in the middle’ of the food chain (food processors, food service operators and retailers), as they have a pivotal role in value chains and can influence consumers’ dietary choices. In line with the ‘ecosystem approach’, other food stakeholders in the wider food system, such as farmers, fishers and other companies as well as consumers and citizens (represented by NGOs), are also very relevant for the Code and will be actively involved in its development, and will continue to play an important role in its implementation.  Based on the developed framework, companies and their representatives will pledge commitments. Commitments will cover the major areas of food sustainability: to promote healthy and sustainable diets by fair marketing practices and limitation of marketing of products high in sugars, fat, and salt; actions to promote animal welfare, enhance biodiversity, reduce food waste and unsustainable packaging, improve water use and energy efficiency, sustainable sourcing of foods and/or ingredients, etc. The Code also fosters a set of ambitious commitments with set targets and measurable impact. Examples of concrete commitments are: to reduce greenhouse gas emissions in scope 1, 2 and 3 by x% by 2030, to increase sales of healthy products and share of plant-based products by x% by 2025, to reformulate foods or to commit to full recyclability, reusability of packaging.  More specifically, the main objectives for the Code are to:   * stimulate the uptake of healthy and sustainable diets; * foster further improvement of internal processes, own operations and organisation in the middle of the food chain; * facilitate sustainable practices by all relevant actors in the food system.   In terms of horizontal objectives, EU associations as well as individual companies in the food system commit to the Code to set a sustainability pathway, to co-design solutions based on best practices, to exchange information with the aim to raise the sustainability bar collectively. |
| **Interaction with sustainable corporate governance** | The Code of Conduct has **synergies with the SCG initiative** as it also targets businesses. The Code mainly targets businesses in the middle of the food chain (food business, retail and hospitality and food service sector) as well as wider in the food system but not all sectors. It contains a set of voluntary, concrete and tangible commitments in relation to the above-mentioned objectives, therefore the Code seeks to encourage businesses to implement sustainable practices that go beyond current regulatory requirements in the environmental, social and “food safety, animal and plant health” area. As it is voluntary, no sanctions are foreseen in case the commitments are breached. Moreover, the businesses are encouraged to also target sustainable practices that are not directly under their responsibility, e.g. encouraging the primary food supply chain to adopt sustainable practices and to avoid negative impacts. As such, a ‘due diligence approach’ is probably part of the Code of conduct. The Code also aims to stimulate companies to encourage their clients to adopt a healthy and sustainable consumption pattern. The Code will not include director’s duties as the commitments will be done either by a group of businesses such as by an association, or by individual companies.  The commitments in the Code will be very concrete in contrast with general principles laid down in the sustainable corporate governance initiative |

# Interaction with EU Trade and Development Cooperation Support Measures

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| --- | --- |
| **Title** | **EU Sustainable Cocoa initiative** |
| **Legislative or non-legislative** | Non-legislative |
| **Description of policy or legislation** | Building on the Living Income Differential introduced by Ghana and Cote d’Ivoire, the two largest cocoa-producing countries, the EU started an ambitious sustainable cocoa initiative focussing that focuses on the three dimensions of sustainability: economic (terms of trade), social (child labour), and environmental (protection of biodiversity, deforestation).  At country level, the initiative will support Western and Central African cocoa producing countries strengthen the institutional, legal and regulatory frameworks for sustainable cocoa production, and empower the private sector, farmers, to improve agricultural practices and comply with sustainability standards. At EU level, the initiative will work towards implementing regulations to eliminate deforestation and socially unacceptable practices in supply chains, supported by a multi-stakeholder dialogue process. |
| **Interaction with sustainable corporate governance** | There will be **synergies** between the Sustainable Cocoa initiative and the SCG initiative. |

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| **Title** | **EU Action Plan on Human Rights and Democracy (2020-2024)** |
| **Legislative or non-legislative** | Non-legislative |
| **Description of policy or legislation** | The Action Plan was adopted by Council in November 2020 and defines the EU priorities on human rights in external action for the years to come.  It includes a commitment for EU and Member States to strengthen engagement in international fora of the United Guiding Principles on Business and Human Rights (UNGPs), and to collaborate with partner countries in actively promoting responsible business conduct. It also seeks to support multi-stakeholder processes (state, business and civil society) to develop, implement and strengthen standards on business and human rights and due diligence. Reflection on how to carry out this work is ongoing. |
| **Interaction with sustainable corporate governance** | **Due diligence is a key aspect of the UNPGs**. Mandatory due diligence requirements will affect the modalities of implementation of the UNGPs in the EU, including the content of an EU comprehensive framework. The extraterritorial dimension of the due diligence requirements is also relevant in this regard. In addition, other aspects possibly covered by the initiative such as liability or access to remedy are also relevant for UNGP implementation. |

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| --- | --- |
| **Title** | **Partnership Instrument (PI) actions on Responsible Business Conduct** |
| **Legislative or non-legislative** | Non-legislative |
| **Description of policy or legislation** | Through the use of Partnership Instrument projects, the EU has created partnerships with international organisations such as the ILO, the OECD, UNDP and the OHCHR. The objective is to provide technical support to develop National Action Plans in Latin America, to **develop tools for the implementation of due diligence in specific sectors, and to promote responsible supply chains in six trading partners in Asia.** |
| **Interaction with sustainable corporate governance** | There are considerable synergies between the SCG initiative and the PI. PI actions aim at promoting corporate due diligence in other parts of the world. This can ultimately facilitate EU companies’ due diligence and lower companies’ costs. Examples:   * Over 20 major agri-businesses with supply chains across the Asian region and reaching Europe were motivated to improve their RBC and due diligence implementation. In Japan, PI support resulted in the development and implementation of the new Guide on Environmental Due Diligence in Value Chain Management under the leadership of the Japanese Ministry of Environment. Thanks to the PI, international standards are now reflected in the Japanese National Action Plan on Business and Human Rights, adopted in October 2020, and the Japanese government committed to promote due diligence in domestic and overseas supply chains. PI actions also contributed to make Thailand the first example of integration of OECD RBC standards in the financial sector in Southeast Asia. For example, the Government Pension Fund, Thailand’s 2nd largest institutional investor ($30 billion assets), has integrated RBC in their policies and documents. In Vietnam, where the textile sector is one of the largest in the country also in terms of exports to the EU, the action allowed to influence the new Textile Strategy, resulting in the inclusion of a sustainability section. In Myanmar PI interventions have considerably contributed to place RBC at the centre of the government agenda and to convince policymakers to institutionalise RBC in the form of the National Action Plan. * The Human Rights Due Diligence and COVID 19: Rapid Self-Assessment for Business tool was adopted by multi-national enterprises such as Daimler AG, and the Brussels-based business association Amfori. * In Latin America, the PI supported the development, or implementation, of NAPs on business and human rights. In Brazil, for example, the link between the Trade and Sustainable Development (TSD) chapter of the EU-Mercosur Association Agreement and the RBC principles is evident, and the project used the Brazilian bid to the OECD as an entry point to promote its agenda. |

The sustainable corporate governance initiative also interlinks with funding from support instruments from other policy areas. Such support measures could be used to facilitate compliance with this initiative. For a list of those measures, please refer to Annex 18.

1. Detailed information on Member State / EEA laws and initiatives

# Member State / EEA laws and initiatives on corporate due diligence in the Supply or value chain

## The following Member States / EEA States have adopted laws on corporate due diligence in the supply or value chain:

* **France**: There is a legal horizontal mandatory due diligence requirement for human rights and environmental impacts through the whole value chain.[[238]](#footnote-239) The law applies to any company which employs at least five thousand employees in its own company and in its direct or indirect subsidiaries whose registered office is located on French territory, or at least ten thousand employees in its own company and in its direct or indirect subsidiaries whose registered office is located on French territory or abroad. Such companies have to establish and implement a vigilance plan based on the UNGPs on an annual basis. The due diligence duty covers the whole supply chain and parent companies are liable for damage that due diligence could have prevented.
* **Netherlands**: A law setting up horizontal mandatory due diligence for child labour concerns through the whole value chain[[239]](#footnote-240) has been adopted but is not yet in force. On 14 May 2019, the Dutch Senate adopted the “Child Labour Due Diligence Law” (“Wet Zorgplicht Kinderarbeid”). Any company established in the Netherlands that sells goods or provides services to Dutch end-users has to determine whether child labour occurs in its supply chain and set out a plan of action on how to combat it. Several aspects of interpretation and especially implementation of the law are still to be determined via General Administrative Order. The law is currently expected to enter into force in 2022.
* **Germany**: A law on horizontal mandatory human rights supply chain due diligence was adopted in June 2021. The law will apply to human rights issues and to limited number of environmental issues, if – because of them – human rights are violated (e.g. in the case of polluted water) or because the company’s activities are not in accordance with certain international environmental agreements. The law applies, from 2023 onwards, to companies with more than 3,000 employees, and from 2024 onwards, to companies with more than 1,000 employees and covers only direct suppliers unless the company had indication about harms occurring among its indirect suppliers.
* **Norway**: A law obliging large and mid-size companies to conduct human rights and decent work conditions due diligence throughout their supply chain was adopted in June 2021. Whilst the law creates a corporate duty to conduct due diligence with respect to human rights and decent work, the scope excludes environmental considerations. This may be reassessed by the Parliament in the future. The law entitles citizens to request information from companies, and the Norwegian consumer authority may issue injunctions and fines for non-compliance. Companies are required to provide or cooperate to ensure remedy, but the law does not provide for civil liability for harm.

## The following Member States have a legislative process ongoing:

* **Austria**: A political party referred a draft bill on social responsibility regarding forced and child labour in the garment sector to the relevant parliamentary committee in June 2020.[[240]](#footnote-241) The aim of the draft is to prevent the placing on the market and distribution of garment products where violations of the prohibition of forced and child labour occur along the production and supply chains.
* **Belgium**: In April 2021, the Belgian parliament voted in favour of considering a bill introducing a duty of care and a duty of responsibility on the part of companies throughout their value chains.
* **Denmark**: A parliamentary motion calls on the Government to introduce a bill on human rights due diligence for all large, as well as companies in high-risk sectors.[[241]](#footnote-242) In January 2019, three Danish political parties presented a parliamentary motion calling the Government to introduce a bill on human rights due diligence for all large, as well as companies in high-risk sectors.
* **Netherlands**: In March 2021, four political parties submitted a draft of a law on Responsible and Sustainable International Business Conduct in Dutch parliament.[[242]](#footnote-243) The law would apply across industry sectors. The law would establish due diligence obligations for any company that knows or can reasonably suspect that its activity can have adverse effects on human rights, labour rights or the environment in a country outside the Netherlands.

## The governments of the following Member States have committed to introducing due diligence legislation[[243]](#footnote-244):

* **Finland**: In June 2020, the Government released a study on possible regulatory options for mandatory due diligence in Finland. The government programme also includes a commitment to promoting due diligence legislation at the EU level.
* **Italy**: Under its National Action Plan on Business and Human Rights, the Government has committed to a review of existing law to assess legislative reform introducing human rights due diligence for companies.
* **Luxembourg**: The 2018 coalition agreement committed to supporting Government initiatives to strengthen the human rights responsibilities of companies.

## In the following Member States, there are Campaigns by civil society organisations:

Ireland

Spain

Sweden

# Member State laws and initiatives on directors’ duties

Company law and the corporate governance framework vary across Member States with respect to specifying if directors should take into account certain stakeholder interests, including long-term interests, when pursuing the interest of the company. The following groups can be distinguished in this regard:

## Expressly regulated by law that specific interests need to be taken into account when directors act in the interest of the company, for instance:

* **France**: the French commercial and civil codes were amended in 2019 to provide that a company needs to be managed taking into account social and environmental challenges[[244]](#footnote-245);
* **The Netherlands**: the Dutch law makes explicit that shareholder interests do not take priority over the interests of other stakeholders;
* **Ireland**: directors have to take into account the interests of employees;
* **Portugal**: directors have to serve the long-term interest of shareholders and also take into account the interests of other relevant stakeholders, such as the employees, customers and creditors.

## No legal requirement but soft law, for instance:

**Belgian** Code on Corporate Governance 2020 [[245]](#footnote-246)

**Dutch** Corporate Governance Code 2016[[246]](#footnote-247)

**German** Corporate Governance Code 2019[[247]](#footnote-248)

**Italian** Corporate Governance Code 2020[[248]](#footnote-249)

**Spanish** Good Governance Code of Listed Companies revised in 2020[[249]](#footnote-250)

## Case law and academic literature provide interpretation, but the outcome differs, for instance:

* **Netherlands**: The Dutch Supreme Court has confirmed that shareholder interests “do not take priority over the interests of other stakeholders” (Dutch Supreme Court ruling in ABN AMRO, 13 July 2007, concerning Book 2, article 140 of the Dutch Civil Code).
* **Spain**: Spanish case law conceives the company's interest as the sum of the individual interests of each of its shareholders (Supreme Court Ruling 120/1991, of 19 February 1991). This Supreme Court Ruling is still referred to in recent rulings, e.g. Supreme Court Ruling 873/2011 of 7 December 2011.
* **Finland:** focuses more on the interest of shareholders
* **Germany and Austria:** focusing more on the interest of stakeholders and even the interest of society.

1. Market context

There are about **13.7 million limited liability companies (LLCs)** in Europe[[250]](#footnote-251).

The vast majority of these are **micro undertakings** within the meaning of the Accounting Directive[[251]](#footnote-252): theyaccount for around **11.6 million** or **85%** of the total[[252]](#footnote-253). Nevertheless, **micro companies** contribute only to about **4% of the total turnover of EU limited liability companies[[253]](#footnote-254)**.

There are an additional **1.8 million small** limited liability companies (excluding micro), constituting about **13%** of the total. These account for roughly **10% of the total turnover**. The share of **medium-sized** limited liability companies from **turnover is about the same**, even though only about **0.2 million or 1.7%** of all limited liability companies fall in this size category. As Annex 11shows, about 40% of medium-sized LLCs operate in economic sectors where the risk that they contribute to environmental or human rights harm is high.

**76 000** limited liability companies are **large**, making up about **0.6%** of the total number of limited liability companies in the EU-27.[[254]](#footnote-255) Around 28 000 (37% of all) large limited liability companies are subsidiaries of other large limited liability companies. Large LLCs generate about **three quarters** of the total turnover of EU limited liability companies[[255]](#footnote-256) and those **with more than 500 employees account for the lion’s share of the turnover** (about 60% of the total), even though only one in every three large limited liability companies meet this employee threshold.

Looking at **very large EU limited liability companies** more closely, from the Orbis database of Bureau van Dijk it appears that about **23 200** companies **have more than 500 employees or a turnover above EUR 350 million**, while roughly **9 400** LLCs have **more than 500 employees and a turnover above EUR 150 million**, andabout **8 900** LLCs have **more than 1000 employees** (irrespective of the turnover).

There are about **3 250** EU limited liability companies that **have shares listed in the EU** (as such, they are covered by the Shareholder Rights Directive). In addition, about **1 740** EU limited liability companies have **only** **bonds** listed in the EU (these are also covered by the Accounting Directive).[[256]](#footnote-257) The total turnover of all EU limited liability companies listed in the EU is a little less than EUR 9 trillion. About one fifth of all listed companies are micro companies, while a **bit more than half are large**; nevertheless, large companies account for 99% of the total turnover generated by EU limited liability companies listed in the EU[[257]](#footnote-258).

According to the Commission’s impact assessment, the sustainability reporting obligations under the Corporate Sustainability Reporting Directive would cover approximately **49 000** companies (including all large companies and all EU and non-EU non-micro companies that have securities listed in EU regulated markets, but accounted for the obligation for corporate groups to report on a consolidated basis).

1. Additional evidence as regards problem definition

# Problem definition, section 2.1.2.: Further examples on how environmental and social matters present risks to the company

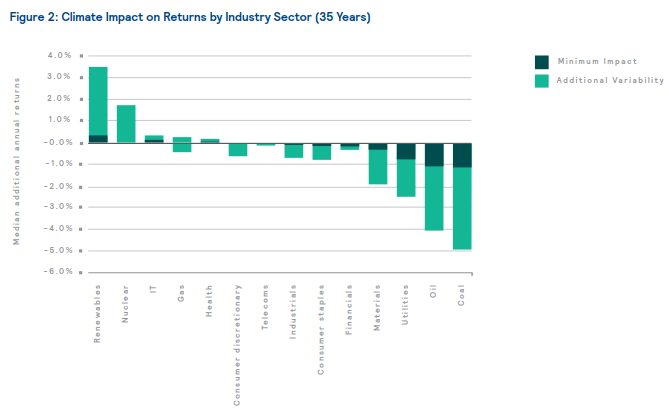
Companies **not properly managing dependencies and risks** stemming from external sustainability factors face challenges to their sustained performance and resilience.

For instance, **climate change-related risks** comprise **physical risks** and **transition risks**.

As regards **physical risks**, primary risks include direct damage to assets (e.g. land, buildings, and infrastructure) due to physical effects of climate change (storms, droughts, fires, etc.). Secondary risks include indirect risks such as availability of key resources, like water, sourcing, quality of raw materials, rising cost of commodities, etc.

The ECB defines **transition risk** as a company’s financial loss that can result, directly or indirectly, from the process of adjustment towards a lower-carbon and more environmentally sustainable economy. This could be triggered, for example, by technological progress or changes in market sentiment and preferences. Transition risks may include risks related to market demands, technology risk, policy risk, reputational risks, etc.

The major **climate transition risks** in volume, according to the Financial Stability Board’s Task Force on Climate Related Disclosures (TCFD)[[258]](#footnote-259) and Bank of England are concentrated in high carbon sectors, that have been identified in the Commission’s [Technical Expert Group’s (TEG)](https://ec.europa.eu/info/publications/sustainable-finance-technical-expert-group_en) report on climate benchmarks and benchmark ESG disclosures[[259]](#footnote-260): agriculture, forestry and fishing, mining and quarrying, manufacturing, electricity, gas, steam and air conditioning supply, water supply, sewerage, waste management, construction, wholesale and retail trade, transportation, real estate. Several central banks have already published some analysis about related risks to the banking sector, including Banque de France[[260]](#footnote-261), Dutch National Bank[[261]](#footnote-262). Mercer’s analysis[[262]](#footnote-263) found that four sectors are far more exposed than others: coal, oil, utilities and materials.



*Source: Mercer (2015), ‘Investing in a time of climate change’*

Other analysis has also been carried out about climate transition risks, for example the Moody’s environmental risks heat map of September 2018 finds that 11 sectors with $2.2 trillion debt have elevated climate risk exposure[[263]](#footnote-264).

**Environmental physical risk, according to the ECB** is[[264]](#footnote-265) the financial impact of a changing climate, including more frequent extreme weather events and gradual changes in climate, as well as of environmental degradation, such as air, water and land pollution, water stress, biodiversity loss and deforestation. Physical risk is therefore categorised as “acute” when it arises from extreme events, such as droughts, floods and storms, and “chronic” when it arises from progressive shifts, such as increasing temperatures, sea-level rises, water stress, biodiversity loss, land use change, habitat destruction and resource scarcity. This can directly result in, for example, damage to property or reduced productivity, or indirectly lead to subsequent events, such as disruptions.

Physical and transition risk drivers impact economic activities and may lead to lower corporate profitability or the devaluation of assets. These risks also affect the resilience of a company’s business model over the medium to longer term, and predominantly those with business models that are reliant on sectors and markets which are particularly vulnerable to climate-related and environmental risks. In addition, physical and transition risks can trigger further losses, stemming directly or indirectly from legal claims (commonly referred to as “liability risk”) and reputational loss (“reputational risk”)[[265]](#footnote-266).

As regards **climate physical risks**, the Commission lists the following sectors as being the most exposed to such risks: infrastructure and buildings, energy, agriculture and forestry, insurance and tourism[[266]](#footnote-267).

**Biodiversity loss** is associated with transition, liability, and physical risks[[267]](#footnote-268). According to the World Economic Forum[[268]](#footnote-269), biodiversity loss is among those risks that dominate in the 5-10 year horizon.[[269]](#footnote-270)

Climate and environmental physical risk can also impact the **supply chain**. For example, semiconductor chips (computers, mobile phones) and rare earths (critical in aerospace and defence, electric vehicles, wind turbines and other electronics) supply chains are highly geographically concentrated in regions with an increasing probability of relevant climate hazards. For semiconductors, hurricanes could lead to months of lost production for the directly affected player and could cause up to 35 percent revenue loss in a disaster year. In the case of rare earths, extreme rainfall in any given year which is sufficient to trigger mine and road closures could roughly double by 2030 in south-eastern China. This could reduce global production by 20 percent in a disaster year[[270]](#footnote-271). Garment company H&M reported to have been hit by record losses due to soaring cotton prices as a result of climate change in India.

Other environmental risks, such as **water-related risks** for example droughts and water scarcity have also been extensively analysed. A recent WWF report[[271]](#footnote-272) shows how droughts and water scarcity could lead to stranded assets in the power and agricultural sectors for example and presents significant risk in the textile sector[[272]](#footnote-273).

Water-related risks affects other sectors as well. For example, climate change-related severe droughts in North-Western Europe in 2018 made navigation on the Rhine river nearly impossible, cutting exporters off from world markets. The disruption reduced German GDP by 0.2 percentage points[[273]](#footnote-274) At the same time, as transport on the Rhine in the third quarter of 2018 was down 27 percent year on year due to low water levels., and transport performance was also 10 percent lower on the Danube, this resulted in a 10 percent drop in Germany’s production of chemicals and pharmaceuticals from September to November, as major industrial players shut down plants that were unable to secure raw material, reporting in some instances over $220 million in additional logistics costs. Another example is water pollution which poses serious risks to businesses. The Climate Disclosure Project (CDP) reports that the apparel and textile sector faces widespread material risks from its contribution to water pollution across the whole value chain.

**Pollution** can also result in significant impact on the company. For example, BP’s Deepwater Horizon 2010 oil spill in the Gulf of Mexico is an example of how environmental risks can have meaningful financial consequences.[[274]](#footnote-275) Social issues and human rights also create risks to the company. For example, the construction, mining, health services and manufacturing sectors are particularly exposed to workplace safety-related risks. Inferior standards can pose a threat to a company’s reputation. Furthermore, companies are increasingly subject to high profile lawsuits for alleged failure to prevent human rights or environmental harms. These cases are often brought against parent companies for the harms caused by their subsidiaries or in their supply chains.[[275]](#footnote-276)

**Reputational** risks can also come in the form of customers or clients choosing not to purchase products or services from the business as consumer preference continue to shift towards sustainability[[276]](#footnote-277).

As regards the magnitude of the problem, **sustainability risks have become more material** for the success of companies in the light of globalisation, climate change, increasing environmental degradation, the resulting scarcity of resources, and growing inequality.[[277]](#footnote-278) Environmental risks are already rated among the ones with the highest likelihood and highest impact risks to businesses, with **human-made** environmental damage perceived as posing an **imminent threat**[[278]](#footnote-279), and based on scientific forecasts, climate change presents increased risks already in the short run.[[279]](#footnote-280) Reputational risks are also increasing as consumer preference continues to shift towards sustainable products.[[280]](#footnote-281)

Some risks affect some **sectors** more than others. For example, climate physical risks affects the most those sectors operating network infrastructures, from energy to telecommunications. The construction, mining, heath services and manufacturing sectors are particularly exposed to workplace-related health and safety risks.

Some **Member States** may be more exposed to some risks, for example draughts and fires in Southern Europe, floods and changing water levels in Central and Western Europe. Other risks may affect all parts of Europe (e.g. SME subcontractors lagging behind the gradual transformation towards climate-friendly production of the buyer). According to the [IPCC report on climate change of 2021](https://www.ipcc.ch/report/ar6/wg1/downloads/report/IPCC_AR6_WGI_Full_Report.pdf), climate change affects all Europe and some parts of Europe are expected to be more affected than other parts of the world.

# Problem Definition, section 2.1.2: Evidence From Corporate Sustainability Reporting practices on Companies’ managing sustainability risks

There is little evidence that companies are managing sustainability risks when **valuing** assets, notably that they take risks resulting from decarbonisation or the physical impacts from climate change into account as they draw up their financial statements.[[281]](#footnote-282)This is despite the fact that the stock of existing assets is at risk because of climate change is large.[[282]](#footnote-283)

The following details on corporate sustainability reporting practices complement the main Impact Assessment report:

As regards specifically the actual and potential impacts of **climate-related risks and opportunities** on the company’s businesses, strategy, and financial planning, large companies’ disclosure remains below 50%[[283]](#footnote-284): 43% of the reviewed 441 EU companies disclose information on climate-related risks and opportunities, 11% disclose information on resilience of their strategies. It is to be noted that [EU climate change reporting guidelines](https://ec.europa.eu/finance/docs/policy/190618-climate-related-information-reporting-guidelines_en.pdf) were published in 2019.

While several large companies are frontrunners, most corporate **strategies** are rarely elaborated with **sustainability objectives** based on **proper measurement**. For example, the TCFD’s 2020 Status Report[[284]](#footnote-285) shows that only 1 in 15 (of the 1700) large companies reviewed disclosed information on the resilience of its strategy. The review found that the percentage of companies disclosing the resilience of their strategies, taking into consideration climate-related scenarios, was significantly lower than that of any other recommended disclosure.

Differences in the corporate sustainability reporting practices across European regions, sizes of companies and sectors are illustrated as follows:

* As regards European regions, the [2020 Research Report of the Alliance for Corporate Transparency](http://allianceforcorporatetransparency.org/assets/Research_Report_EUKI_2020.pdf), an analysis of the sustainability disclosures of 300 companies from Central, Eastern and Southern Europe under the NFRD, finds that companies from Central, Eastern and Southern Europe have less complete reporting practices than Western and Northern European peers.
* As regards sizes of companies, according to the TCFD’s 2020 Status Report, referred to above, much fewer companies with 3 B USD market capitalisation report than those with market capitalisation of more than 10 B USD. Further as regards sizes of companies, in the [Global Reporting Initiative’s Sustainability Disclosure](https://database.globalreporting.org/search/) [Database](https://database.globalreporting.org/search/) only between 10-15% of all sustainability reports in 2017-18 came from SMEs. Literature shows that most SMEs have been slow to adopt environment-related improvements in the EU. Only 29% of SMEs have introduced measures to save energy or raw materials (46% of large enterprises) and only 4% have a comprehensive energy efficiency system in place (19% of large enterprises).[[285]](#footnote-286)
* As regards sectors, climate-related reporting aligned with 1.5˚C or well below 2˚C is more present in the energy and resource extraction sector (22%), than in the resource transformation, financial, transportation, infrastructure sectors (between 2.6 and 8.2%).[[286]](#footnote-287)

# Problem definition, section 2.1.3: Further examples illustrating how EU companies’ value chains and own operations adversely impact human rights and the environment

* In the garment sector, recent reports of the use of **forced labour** of Uyghurs in the cotton production in Xinjiang have revealed great risks of human rights violations. The Xinjiang province in China is said to produce almost 20% of global cotton supplies[[287]](#footnote-288). It is therefore likely that thousands of EU companies are using such cotton in their garment production.[[288]](#footnote-289)
* The EU automobile and cosmetic sectors have also been linked to **forced labour** in India and Madagascar, from which they solely source mica mineral[[289]](#footnote-290).
* **Support for non-state armed groups and child labour** has been reported not only in the minerals sector, i.e., in mining communities in the DRC but also across multiple other countries[[290]](#footnote-291).[[291]](#footnote-292)
* **Child labour** in cocoa supply chains in Ghana and Côte d’Ivoire,[[292]](#footnote-293) from which the largest proportion of cocoa products are exported to the EU.[[293]](#footnote-294)
* Consumption by EU Member States of clothing, textiles and leather products is reported[[294]](#footnote-295) to have contributed in 2015 to around 375 fatal **accidents** and 21,000 non-fatal accidents **due to poor working conditions** in supply chains outside the EU.
* **Violations of labour rights and exploitation of workers**, including migrant workers, have been documented in the EU manufacturing industry and telecommunication services including inside the EU, particularly in the manufacturing industry, the agricultural sector and the construction sector[[295]](#footnote-296).
* EU production and consumption patterns have been linked to **environmental pressures** in other parts of the world.[[296]](#footnote-297)
* By 2015, a share of at least 30% of the GHG emissions from EU consumption were due to emissions embodied in imports.[[297]](#footnote-298) Value chain emissions, both upstream and downstream, account for more than 70% of total emissions in manufacturing and can reach 95% in the oil and gas industry[[298]](#footnote-299).
* Activities of the subsidiaries of multinational EU companies led to the **pollution** of the environment resulting in the loss of livelihoods and health for local communities.[[299]](#footnote-300)
* EU multinational companies in the mining and energy sectors disposing **of industrial waste** by subcontractors in developing countries without adequate treatment.[[300]](#footnote-301)

1. High- impact sectors and number of medium-sized and large companies operating in those sectors

This Annex discusses various possibilities for the identification of high-impact sectors. The final list of sectors could be based on one of these options or on another one including a combination of sectors contained in the list. The largest list of sectors should be interpreted as the largest possible one and, enables to calculate the maximum impact of the economy that such a list would have.

# Options for the definition of high-impact sectors

A possible **basic list could include** **some key sectors** that are already covered by the OECD due diligence guidance as well as on targeted lists aiming at addressing serious violations of human rights such as forced labour and child labour risks, e.g. the US Department of Labour list on goods produced with forced labour and child labour. Some key sectors like agriculture, garment, mining and extraction overlap in all these lists and such overlap is explained by the fact that cases of serious violations of human rights have been registered in this sector by international organisation, other public organisations and also national authorities who have included these sectors (except for jewellery) in the prioritization of their action. Some of these sectors, notably agriculture and mining, are included in the Commission`s staff working document on Decent Work. Whilst these sectors could be considered, on these basis, as a core group of sectors, other sectors like jewellery and consumer electronics could be covered precisely to address a priority risks like child labour and forced labour. This could be a first step of a phase-in approach. Further sectors can be added at a later stage, through the empowerment of the Commission to extend the list.

A **second list** would cover, in addition to the sectors mentioned above**, important sectors included in the** EU Emissions Trading System regulation and from the Benchmark delegated regulation looking at environmental impacts.

The **third list** is a “maximum list” of sectors that can be regarded as high-impact from an environmental and/or human rights perspective. In addition to the sectors covered by the two above mentioned lists, this third list covers other sectors based on different initiatives establishing sectoral and cross-sectoral sustainability standards and monitoring of value chains (these can be regarded as indicating the sectors with the high risk of adverse human rights impacts), NGO reports, the Commission Staff Working Document “[Promote Decent Work Worldwide Responsible Global Value Chains For A Fair, Sustainable And Resilient Recovery From The Covid-19 Crisis](https://ec.europa.eu/social/BlobServlet?docId=23131&langId=en)” (2020), studies prepared for sectoral dialogues in the Netherlands and Germany, as well as the OECD Database of cases with a complaint on human rights issues brought to OECD National Contact Points. See details later in this annex.

For adverse **impact on climate and the environment**, the sectors with the highest GHG emissions based on the **entire** **EU Emissions Trading System (EU ETS)** **list** are **included**. This covers sectors with high impact on climate change in the own operations within the EU. However, the ETS list of sectors does not cover sectors where supply chain emissions are high. Therefore, **the list is complemented by sectors identified in the Commission Delegated Regulations adopted for the EU Benchmarks Regulation**[[301]](#footnote-302). These also scope all “scope 3” GHG emissions data (i.e. emissions in the value chain and of the product) in the benchmark methodology and identify the most relevant sectors, notably manufacturing, construction and transport. Sectors were then further specified based on Eurostat and European Environment Agency data. Furthermore, we relied on the EU Taxonomy Regulation, in particular for identifying sectors where the risk of other negative environmental impact is high (i.e. beyond climate change impact).

| Option for defining high-impact sectors | Selection criteria | Sectors covered | Total number of individual medium-sized and midcap companies covered[[302]](#footnote-303) |
| --- | --- | --- | --- |
| 1. Basic list | **Some limited key sectors** with existing OECD due diligence guidance and the US Department of Labour list on goods produced with forced labour and child labour are covered. | Agriculture, forestry and fishing  Manufacture of textile, wearing apparel and footwear  Mining and quarrying, minerals, including extraction of petroleum and gas  Consumer electronics (Manufacture of electronic components and boards; of computers and peripheral equipment; of communication equipment)  Manufacturing of jewellery, bijouterie and related articles  Manufacture of food and beverages | 10 200  (7140) |
| 1. Medium list | **Important sectors** from the EU Emissions Trading System regulation and from the Benchmark delegated regulation looking at environmental impacts as well as and the US Department of Labour list on goods produced with forced labour and child labour. | Agriculture, forestry and fishing  Manufacture of textile, wearing apparel and footwear    Mining and quarrying, minerals  Manufacture of coke and refined petroleum products  Iron, steel, cement manufacturing  Manufacture of chemicals and chemical products  Manufacture of food and beverages  Construction  Consumer electronics (Manufacture of electronic components and boards; of computers and peripheral equipment; of communication equipment)  Wholesale of agricultural raw materials and live animals; of food, beverages and tobacco; of household goods; of information and communication equipment  Manufacture of jewellery, bijouterie and related articles | 30 993  (21 695) |
| 1. Maximum list | High-impact sectors as regards human rights: based on existing evidence, including  as well as and the US Department of Labour list on goods produced with forced labour and child labour, Commission Staff Working Document “[Promote Decent Work Worldwide Responsible Global Value Chains For A Fair, Sustainable And Resilient Recovery From The Covid-19 Crisis](https://ec.europa.eu/social/BlobServlet?docId=23131&langId=en), and OECD guidance.  Broader range of high climate impact sectors covered by the ETS regulation, the Benchmark delegated regulation and further sectors identified based on Eurostat and EEA data and on the basis of the Taxonomy regulation | Agriculture, forestry and fishing  Mining and quarrying  Manufacture of food products and beverages  Manufacture of textiles, wearing apparel, footwear  Manufacture of wood and of products of wood and cork, except furniture; manufacture of articles of straw and plaiting materials  Manufacture of paper and paper products  Manufacture of coke and refined petroleum products  Manufacture of chemicals and chemical products  Manufacture of rubber and plastic products  Manufacture of other non-metallic mineral products  Manufacture of basic metals  Manufacture of fabricated metal products, except machinery and equipment  Manufacture of electronic components and boards  Manufacture of computers and peripheral equipment  Manufacture of communication equipment  Manufacture of machinery and equipment n.e.c.  Manufacture of jewellery, bijouterie and related articles  Manufacture of games and toys  Electricity, gas, steam and air conditioning supply  Water collection, treatment and supply  Waste treatment and disposal  Construction  Wholesale of agricultural raw materials and live animals  Wholesale of food, beverages and tobacco  Wholesale of household goods  Wholesale of information and communication equipment  Water transport  Air transport  Information service activities | 49 486  (34 640) |

# Indicative maximum list of high-impact sectors

The following table lists those sectors and subsectors of the economy which, based on the information available to the Commission at this stage, could be regarded as high-impact from an environmental and/or human rights perspective. This list is indicative and has been compiled solely for the purposes of estimating the impacts on companies in the relevant options.

The table also shows maximum number of companies that could potentially fall under the targeted regime *in addition* to the large or very large companies that are covered by the scope under these options irrespective of the sector of their main activities.

Accordingly, the table compiles:

(i) the number of **medium-sized** limited liability companies, defined in a simplified manner as companies with employees between 50 and 250 and a turnover between EUR 8 and 40 million (option 4 under due diligence);

(ii) the number of **medium-sized and midcap** limited liability companies according to the two different definitions (above which size the full due diligence obligation applies, see options 3a and 3b).

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| NACE Code | NACE Label | Medium-sized:  50-250 and 8m-40m  (opt. 4, incl. in opt. 3a-b) | Medium-sized and midcaps def. 1:  50-500 and 8m-350m  (opt. 3a) | Medium-sized and midcaps def. 2: 50+ and 8m+ but excl. 500+ and 150m+  (opt. 3b) |
| A | Agriculture, forestry and fishing | 781 | 1.040 | 1.090 |
| B | Mining and quarrying | 253 | 425 | 475 |
| C10 | Manufacture of food products | 2.568 | 4.689 | 4.986 |
| C11 | Manufacture of beverages | 301 | 586 | 626 |
| C13 | Manufacture of textiles | 677 | 1.005 | 1.057 |
| C14 | Manufacture of wearing apparel | 380 | 580 | 656 |
| C152 | Manufacture of footwear | 224 | 311 | 337 |
| C16 | Manufacture of wood and of products of wood and cork, except furniture; manufacture of articles of straw and plaiting materials | 659 | 992 | 1.032 |
| C17 | Manufacture of paper and paper products | 694 | 1.210 | 1.254 |
| C19 | Manufacture of coke and refined petroleum products | 33 | 103 | 124 |
| C20 | Manufacture of chemicals and chemical products | 1.057 | 2.199 | 2.309 |
| C22 | Manufacture of rubber and plastic products | 2.022 | 3.059 | 3.198 |
| C23 | Manufacture of other non-metallic mineral products | 1.093 | 1.737 | 1.874 |
| C24 | Manufacture of basic metals | 695 | 1.398 | 1.508 |
| C25 | Manufacture of fabricated metal products, except machinery and equipment | 3.665 | 4.994 | 5.179 |
| C261 | Manufacture of electronic components and boards | 292 | 482 | 533 |
| C262 | Manufacture of computers and peripheral equipment | 75 | 129 | 145 |
| C263 | Manufacture of communication equipment | 115 | 189 | 205 |
| C28 | Manufacture of machinery and equipment n.e.c. | 2.935 | 4.685 | 4.908 |
| C321 | Manufacture of jewellery, bijouterie and related articles | 51 | 87 | 89 |
| C324 | Manufacture of games and toys | 36 | 54 | 62 |
| D | Electricity, gas, steam and air conditioning supply | 379 | 977 | 1.165 |
| E36 | Water collection, treatment and supply | 250 | 433 | 517 |
| E382 | Waste treatment and disposal | 204 | 325 | 343 |
| F | Construction | 5.427 | 7.410 | 7.661 |
| G462 | Wholesale of agricultural raw materials and live animals | 117 | 323 | 346 |
| G463 | Wholesale of food, beverages and tobacco | 1.441 | 2.597 | 2.759 |
| G464 | Wholesale of household goods | 1.525 | 3.210 | 3.393 |
| G465 | Wholesale of information and communication equipment | 331 | 737 | 820 |
| H50 | Water transport | 114 | 214 | 241 |
| H51 | Air transport | 52 | 126 | 138 |
| J63 | Information service activities | 286 | 412 | 456 |
| TOTAL (high-impact sectors, EU27) | | **28.732** | **46.718** | **49.486** |
| Total other (all non high- impact sectors, EU27) | | 37.293 | 61.230 | 69.321 |
| TOTAL (all sectors, EU27) | | 66.025 | 107.948 | 118.807 |
| Coverage (total in high-impact / total in all sectors) | | 44% | 43% | 42% |

*Source: Orbis database of Bureau van Dijk. Please note that the data were extracted from flat files downloaded in September 2021, using Bureau van Dijk’s own categorisation of limited liability company forms and the size categories relevant for the two policy options (which are slightly different from the definitions in the Accounting Directive). We included only those firms in the sample for which the latest available information in Orbis stems from 2014 or later (up until 2018). The total number of such companies in the given high-impact sectors is 606 500 in Orbis, while Eurostat’s Structural Business Statistics contain 5 437 000 business enterprises in these sectors (excluding agriculture). The large difference can be attributed to various reasons, including the differences in the data collection method and the statistical units used, and the inclusion of only active enterprises. Nevertheless, the difference is much smaller in the medium to large company size categories, which is in the focus of our analysis: according to Eurostat, there are about 37 000 enterprises with employees between 50 and 250 in these high-impact sectors (excluding the agricultural sector).*

# Methodology for selecting high-impact sectors

In the following points we explain in detail the methodology applied to define high impact sectors for climate change and environmental impact.

## Sectors covered by the EU ETS

The most recent **EU Emissions Trading System data from the European Environment Agency[[303]](#footnote-304)** lists the economic sectors and economic activities that are covered in the EU carbon market. The following sectors are covered (with the corresponding indicated):

|  |  |
| --- | --- |
| ETS sectors | NACE codes |
| Fuel combustion (mainly electricity generation plus various manufacturing industries) | D.35 Electricity, gas, steam and air conditioning supply |
| Refineries | C.19.2 Manufacture of refined petroleum products |
| Iron and steel, coke, and metal ore production | C.19.1 Manufacture of coke oven products /  B.07 Mining of metal ores /  C.24 Manufacture of basic metals  (including C.24.42 - Aluminium production) |
| Cement, clinker and lime production | C.23.5 Manufacture of cement, lime and plaster /  C.23.6 Manufacture of articles of concrete, cement and plaster |
| Other non-metallic minerals (glass, ceramics, mineral wool and gypsum) | C.23 Manufacture of other non-metallic mineral products  (including C.23.1 Manufacture of glass and glass products; C.23.3 Manufacture of clay building materials /  C.23.4 Manufacture of other porcelain and ceramic products) |
| Production of pulp and paper | C.17 Manufacture of paper and paper products |
| Production of chemicals | C.20 Manufacture of chemicals and chemical products |
| Other (opt-ins and capture of GHGs): Transport of GHG | H.49.5 Transport via pipeline |
| Aviation (partly) | H.51 Air transport |

Importantly, the document further states: “The majority of the stationary installations in the EU ETS are fuel combustion plants (63%) (…). In terms of emissions, the cement, clinker and lime production sector is the second largest sector (10% of emissions), even though it ranks fourth in terms of the number of installations. Both the iron, steel and coke sector and the refinery sector account each for 9% respectively 8% emissions from stationary installations, followed by the chemicals sector, responsible for 5% of emissions.”

The EU ETS today represents approximately half of EU’s total GHG emissions. It is focused on the most-emitting sites and does not yet cover, or will cover only at later stage, three important sectors where emissions are much more diffuse: i.e. transport, buildings and agriculture. Therefore, it is necessary to complete the EU ETS list with other relevant EU sources in order to capture all relevant high-carbon sectors.

## Benchmark Regulation

The Benchmark Regulation[[304]](#footnote-305) was amended, in the framework of the EU Sustainable Finance Action Plan, to create two climate benchmark categories and to require sustainability disclosure to benchmark providers. The level 1 regulation required the development of several Delegated Acts. Two of these Delegated Acts are quite relevant to define high-carbon sectors:

1. Commission Delegated Regulation (EU) 2020/1816 supplementing Regulation (EU) 2016/1011 as regards the explanation in the benchmark statement of how environmental, social and governance factors are reflected in each benchmark provided and published.

Annex II on ESG factors to be considered by underlying assets of the benchmark: Section 1 on Equity refers to “Exposure of the benchmark portfolio to companies the activities of which fall under Divisions 05 to 09, 19 and 20 of Annex I to Regulation (EC) No 1893/2006.”. In order to ensure consistency, these sectors should be integrated in the definition of “high-carbon sectors”:

Divisions 05 to 09 and 19 and 20 of Annex I to Regulation (EC) No 1893/2006 correspond to the following NACE codes:

B.05 Mining of coal and lignite

B.06 Extraction of crude petroleum and natural gas

B.07 Mining of metal ores

B.08 Other mining and quarrying

B.09 Mining support service activities

C.19 Manufacture of coke and refined petroleum products

C.20 Manufacture of chemicals and chemical products

2. Commission Delegated Regulation (EU) 2020/1818 supplementing Regulation (EU) 2016/1011 as regards minimum standards for EU Climate Transition Benchmarks and EU Paris-aligned Benchmarks.

Article 5 on Phase-in of Scope 3 GHG emissions data in the benchmark methodology sets out (underlining added):

“1. The benchmark methodology for EU Climate Transition Benchmarks or EU Paris‑aligned Benchmarks shall include Scope 3 GHG emissions data in the following way:

(a) As of the date of application of this Regulation, Scope 3 GHG emissions data for at least the energy and mining sectors referred to in Divisions 05 to 09 and 19 and 20 of Annex I to Regulation (EC) No 1893/2006;

(b) within two years from the date of application of this Regulation, Scope 3 GHG emissions data for at least the transportation, construction, buildings, materials and industrial sectors referred to in Divisions 10 to 18, 21 to 33, 41, 42 and 43, 49 to 53 and Division 81 of Annex I to Regulation (EC) No 1893/2006;

(c) within four years from the date of application of this Regulation, Scope 3 GHG emissions data for all other sectors referred to in Annex I to Regulation (EC) No 1893/2006.”

The NACE codes of the additional sectors are as follows:

C.10 Manufacture of food products

C.11 Manufacture of beverages

C.12 Manufacture of tobacco products

C.13 Manufacture of textiles

C.14 Manufacture of wearing apparel

C.15 Manufacture of leather and related products

C.16 Manufacture of wood and of products of wood and cork, except furniture; manufacture of articles of straw and plaiting materials

C.17 Manufacture of paper and paper products

C.18 Printing and reproduction of recorded media

C.21 Manufacture of basic pharmaceutical products and pharmaceutical preparations

C.22 Manufacture of rubber and plastic products

C.23 Manufacture of other non-metallic mineral products

C.24 Manufacture of basic metals

C.25 Manufacture of fabricated metal products, except machinery and equipment

C.26 Manufacture of computer, electronic and optical products

C.27 Manufacture of electrical equipment

C.28 Manufacture of machinery and equipment n.e.c.

C.29 Manufacture of motor vehicles, trailers and semi-trailers

C.30 Manufacture of other transport equipment

C.31 Manufacture of furniture

C.32 Other manufacturing

C.33 Repair and installation of machinery and equipment

F.41 Construction of buildings

F.42 Civil engineering

F.43 Specialised construction activities

H.49 Land transport and transport via pipelines

H.50 Water transport

H.51 Air transport

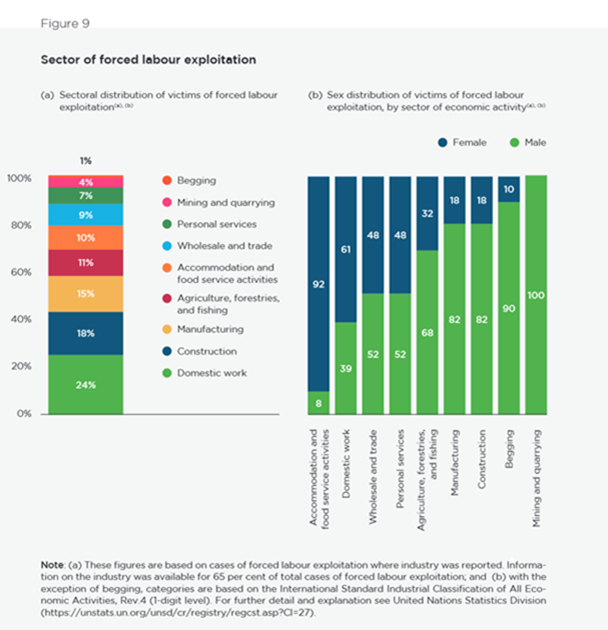
H.52 Warehousing and support activities for transportation

H.53 Postal and courier activities

N.81 Services to buildings and landscape activities

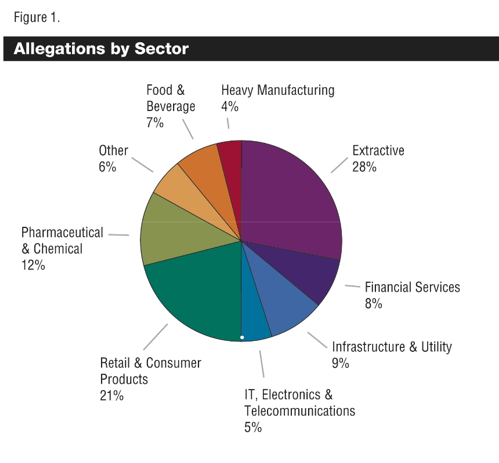
As regards the methodology to define **high-impact sectors for human rights abuses**, different sources were considered including in particular the following:

Commission Staff Working Document “[Promote Decent Work Worldwide Responsible Global Value Chains For A Fair, Sustainable And Resilient Recovery From The Covid-19 Crisis](https://ec.europa.eu/social/BlobServlet?docId=23131&langId=en)” (2020). According to this, globally 12% of child labour is in industry and mining, 17% in services and 71% in agriculture, fishing and forestry.

Alliance 8.7 – [Global estimates of modern slavery: forced labour and forced marriage](https://www.ilo.org/wcmsp5/groups/public/@dgreports/@dcomm/documents/publication/wcms_575479.pdf) (2017):

[Annual lists (latest from 2020)](https://www.dol.gov/sites/dolgov/files/ILAB/child_labor_reports/tda2019/2020_TVPRA_List_Online_Final.pdf) of the US Department of Labor on goods produced with forced and child labour, which give an indication of most affected sectors per country,

[ITC Standards Map](https://www.standardsmap.org/standards_intro), which provides comprehensive, verified and transparent information on standards for environmental protection, worker and labour rights, economic development, quality and food safety as well as business ethics (260 different sustainability standards) across the following sectors: agriculture, consumer products, electronics, fish (wild & aquaculture), forestry, industry, jewellery, livestock, mining, processed food, services, textile/markets;

A 2008 [survey](https://media.business-humanrights.org/media/documents/files/reports-and-materials/Ruggie-2-addendum-23-May-2008.pdf) conducted for Professor John Ruggie, SRSG for Business and Human Rights, on the scope and patterns of corporate abuse of human rights that provided input into the development of the UNGPs, 

[CSR Sector Risk Assessment](https://www.imvoconvenanten.nl/-/media/imvo/files/mvo-sector-risk-assessment.pdf?la=en&hash=E04F2533DE30CFF10A2C2D3C2E2D1327) for **Dutch Responsible Business Conduct Covenants**, commissioned by the Dutch Minister for Foreign Trade and Development Cooperation and the Minister of Economic Affairs, prepared by KPMG (2014);

[Respect for Human Rights along Global Value Chains](https://www.adelphi.de/en/project/industry-study-business-and-human-rights), prepared by [**Adelphi and EY for the German Federal Ministry of Labour and Social Affairs**](https://www.adelphi.de/de/system/files/mediathek/bilder/fb-543-achtung-von-menschenrechten-entlang-globaler-wertschoepfungsketten.pdf)**.[[305]](#footnote-306)**

[Sectors covered by the OECD sectorial guidance on due diligence](https://mneguidelines.oecd.org/sectors/)[[306]](#footnote-307) (besides finance as this sector is covered by EU Sustainable Finance Package already).

# Companies belonging to a group or a value chain already covered

**Many of the high-impact midcaps and medium-sized companies are part of the groups or value chains of larger companies** and will most likely be indirectly impacted by the obligations of those companies that fall under the scope of the full due diligence obligation (large or very large companies, depending on the option). The due diligence requirement applying to the large (or very large) company (i.e. identification and prevention of *all* adverse impacts throughout subsidiaries and value chains) and to its value chain suppliers operating in high-impact sectors (i.e. identification and prevention of *relevant* adverse impacts) would be **inconsistent**.

For the purposes of cost calculation the number of midcaps and medium-sized high-impact companies falling under the risk-based regime we consider those companies which would not be already affected, i.e. which are not part of other, large (or very large) companies’ groups. This does not mean that subsidiaries would not have costs, but those costs would be indirect. As regards how many midcaps or medium-sized companies are subsidiaries of large (or very large) companies there are no conclusive data.

Regarding groups, the CEPS study on the NFRD shows that 9% of the EU LLCs are subsidiaries of other EU LLCs, and that this ratio is largest for large LLCs (37%) and for medium-sized LLCs (about 31%)[[307]](#footnote-308).

To sum up, for the purposes of calculating the cost of due diligence **the number of midcaps and medium-sized companies (option 3 under due diligence) or only medium-sized companies (option 4 under due diligence) that would presumably not bear significant additional costs as they would already be indirectly impacted by the initiative through the obligation of their larger parent companies to undertake full due diligence**, we can approximately assume that **30%** of those companies are already part of group of a larger company. This means that the total number of companies covered would be:

| **Medium-sized:**  LLC\_50\_250\_empl\_and\_8\_40\_turn  **(option 4, also incl. in options 3a, 3b)** | **Midcaps and medium-sized companies (def. 1)**  LLC\_50\_500\_empl\_and\_8\_350\_turn  **(option 3a)** | **Midcaps and medium-sized companies (def. 2):** LLC\_50plus\_empl\_and\_8plus\_turn but excl. LLC\_500plus\_emply\_and\_150plus\_turn  **(option 3b)** |
| --- | --- | --- |
| 20 112 | 32 702 | 34 640 |

As regards companies belonging to the value chains of very large or large companies, we calculate with the cost of targeted due diligence. Although these companies will be indirectly affected by the obligation of the large buyer company, in reality the efforts that they need to carry out for compliance may be more limited than the cost of targeted due diligence. As there is no precise estimate, we presume that the cost numbers used are a conservative estimate.

1. European Parliament reports

The European Parliament (EP) adopted two complementary own initiative reports prepared by the Committee on Legal Affairs (JURI) in support of the objectives of the Commission to foster long-term corporate behaviour towards the sustainability transition:

* [European Parliament non-legislative resolution of 17 December 2020 on sustainable corporate governance](https://www.europarl.europa.eu/doceo/document/TA-9-2020-0372_EN.html)([2020/2137(INI)](https://www.europarl.europa.eu/doceo/document/TA-9-2020-0372_EN.html), rapporteur Pascal Durand, Renew/FR)
* [European Parliament resolution of 10 March 2021 with recommendations to the Commission on corporate due diligence and corporate accountability](https://www.europarl.europa.eu/doceo/document/TA-9-2021-0073_EN.html) (2020/2129(INL), rapporteur Lara Wolters, S&D/NL)

In its **non-legislative resolution of 17 December 2020 on sustainable corporate governance**, the EP expressed the view that corporate governance has a key role to play in delivering on the EU’s international sustainability commitments and in achieving a resilient and sustainable economy. The EP found that voluntary and soft law initiatives to promote sustainable corporate governance had largely proven to be ineffective in changing corporate behaviour towards sustainability. Accordingly, the EP called for new EU legislation on directors’ duties in order to strengthen the role of directors in pursuing the long-term interests of companies and to ensure the integration of sustainability – including human rights and environmental concerns – into corporate decision-making. At the same time, the EP considered that the Commission should propose new EU legislation both on corporate due diligence obligations and directors’ duties, emphasising the need for both as they are complementary but not interchangeable.

A large part of the points raised in the resolution are covered by the on-going Commission’s work preparing an EU initiative on sustainable corporate governance. More specifically, in response to the EP suggestions, in its impact assessment, the Commission proceeded as follows:

* Assessed policy options that could ease short-term pressure on directors and ensure that sustainability aspects are properly integrated into corporate decision-making, including the option of harmonisation by an EU directive.
* Considered how to ensure sufficient flexibility and proportionality to avoid unnecessary red tape.
* Assessed various options as regards the scope of the initiative. In this context, due consideration was given to limiting and alleviating the burden for SMEs and providing accompanying measures to ease the implementation by businesses.
* Reflected on the possibility to include large limited liability companies, and medium-sized companies which are active in sectors of economic activity where the risk of having a significant impact on sustainability matters is high. With regard the suggestion to identify all sectors of economic activity that have a significant impact on any sustainability matters, the costs and benefits of such a solution were carefully assessed.
* Considered the possibility of specific guidance and other supporting measures for companies and in particular to SMEs if they should fall under the scope or of sector-specific guidance, reflecting on the request to specifically target sectors that are often linked with certain illegal business activities.
* Noted the specific proposal to ensure that employees’ rights to vocational training and lifelong education are guaranteed effectively, by clarification of the directors’ duties to act in the interest of the company and to integrate sustainability aspects in the strategy, which would contribute to the recognition and promotion of such rights by the directors.
* Explored how to align corporate activities to the EU’s overall climate-neutrality and other environmental objectives by assessing the possibility to require directors to include in the corporate strategies measurable, specific, time-bound and science-based sustainability targets, and to align these with the EU’s international commitments under the Paris Agreement, the Convention on Biological Diversity and international agreements addressing deforestation.
* Noted the need to ensure that companies possess financial securities for environmental liability for environmental harm inflicted on individuals and ecosystems as the sustainable corporate governance initiative would aim at preventing such harm and also ensuring that the risk posed by a failure to do so is identified and managed properly.
* Noted the request to interpret stakeholders in a broad sense and to consider a requirement to consult the local public authorities responsible for employment and environmental public policies by exploring how workers’ representatives and other relevant stakeholders should be informed, consulted or involved in corporate decision-making, including in identifying and assessing the significance of actual and potential sustainability impacts and in defining and monitoring sustainability-related aspects of strategies.
* Considered the option of requiring companies, depending on their size and field of activity, to set up advisory committees, comprising representatives of employees and other stakeholders as well as independent experts, with the aim of providing advice to the board on the integration of sustainability in the strategy while playing a role in monitoring or enforcing the implementation of the sustainability-related elements of the strategy.
* Included certain non-EU companies under the scope of the initiative.

In its **resolution of 10 March 2021 with recommendations to the Commission on corporate due diligence and corporate accountability**, the EP requested the Commission to adopt a Directive on Corporate Due Diligence and Corporate Accountability and two complementary proposals to amend the ‘Brussels Ia Regulation’ and the ‘Rome II Regulation’ as regards access to justice before EU courts and the application of EU law for civil claims for human rights violations. The report proposes EU rules on value chain due diligence obligations for undertakings, namely to take all proportionate and commensurate measures to prevent adverse impacts on human rights, including labour and social rights, the environment and good governance from occurring in their value chains, and to properly address such adverse impacts when they occur. More specifically, the report proposed to:

* align the definition of human rights and environmental harm with international human rights and environmental conventions and EU environmental standards consistent with the Union’s objectives on environmental protection and climate change mitigation[[308]](#footnote-309).
* include in the scope large companies, listed SMEs and high-risk SMEs as well as third-country companies when they operate in the EU internal market selling goods or providing services.
* broadly define due diligence, including all efforts to assess whether undertakings’ own operations and business relationships cause or contribute to or are directly linked to potential or actual adverse impacts.
* require undertakings to establish a due diligence strategy, unless they conclude that they do not cause or contribute to or are not directly linked to potential or actual adverse impacts. Undertakings would be obliged to make the due diligence strategy or the assessment that no impacts are caused publicly available, especially on their websites.
* include provisions on stakeholder engagement, with particular focus on trade unions and workers’ representatives, as well as provisions on grievance mechanisms and extra-judicial remedies.
* ensure supervision by national competent authorities designated by Member States. Among the sanctions – in case of irreparable harm – the temporary suspension of activities may be ordered or in case of a third country company, a ban on operating in the internal market.
* require Member States to have a liability regime in place for harm arising out of potential or actual adverse impacts on human rights, the environment and good governance that companies cause or to which they contribute in their value chain.
* introduce further sector-specific EU mandatory due diligence legislation, for example for sectors such as forest and ecosystem risk commodities and the garment sector.

A large part of the points raised in the resolution are covered by the on-going Commission’s work preparing an EU initiative on sustainable corporate governance. More specifically, in response to the EP suggestions, in its impact assessment, the Commission proceeded as follows:

* Adopted a broad concept of due diligence obligation as this is in line with relevant international standards that the Commission supports.
* Took note of the proposal for inclusion of listed and high-risk SMEs next to large companies and considered ways of limiting and alleviating the burden for SMEs in accordance with Better Regulation rules.
* Took note of the recommendation for supervision by designated national authorities which corresponds to the necessary case- and risk-based analysis as regards compliance with due diligence.
* Took note of the proposed harmonisation at EU level by means of a specific obligation for Member States to provide for a civil liability regime. However, the content of the liability regime proposed in the report is limited to causing or contributing to the harm, therefore covering only part of the proposed due diligence duty, mostly first tier suppliers. Such limitation does not correspond to the due diligence concept of existing international standards (e.g. OECD guidelines, United Nations Guiding Principles on Business and Human Rights). It also may fall short of covering in particular important risks to the environment as well as regards human rights, including labour and social rights (e.g. forced labour) that tend to materialise in supply chains beyond tier one suppliers.
* Paid due attention to consistency, for example with complementary proposal (CSRD -review of the Non-Financial Reporting Directive, deforestation initiative, environmental EU law etc.)
* As regards the proposal to also address international private law matters in the upcoming initiative, considered that relevant private international law aspects should in general not be addressed in a specific instrument on sustainable corporate governance but in the horizontal instruments on private international law, i.e. the Brussels Ia and Rome II Regulations.

In conclusion, both complementary reports are in line with the Commission’s political priorities of moving to a transformation towards more sustainable economy, including sustainable corporate governance that can contribute to companies’ resilience and performance in the long term. They confirm the momentum for the ongoing work towards a legislative proposal on sustainable corporate governance. This work will be an important contribution to the objectives of the European Green Deal, as well as for the EU’s international commitments, while also underline the need to ensure EU industry competitiveness and recovery as we emerge from the current crisis.

1. Detailed Description of Available Policy Options on Due Diligence and Directors’ Duties

# Options for Corporate Due Diligence

## Discarded options on due diligence and their analysis

### Non-regulatory measures

This option would entail **new voluntary guidelines or a recommendation** at EU level for companies on undertaking due diligence through their value chains.

Voluntary due diligence regimes play a role in promoting the implementation of responsible business practices. Guidelines may be taken into account to some extent in civil claims and in contracts. They may also be more flexible than mandatory harmonised rules.

Examples of internationally recognised guidelines in this context include the UNGPs, and the OECD Guidelines for Multinational Enterprises[[309]](#footnote-310) and further embedded in the recommendations of ILO Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy.[[310]](#footnote-311) Industry has also produced guidance documents on responsible business conduct and due diligence.[[311]](#footnote-312) A new EU horizontal guidance on due diligence for sustainability impacts could build on the mentioned existing standards and strengthen their promotion at EU level.

However, voluntary guidelines would have a limited impact in changing corporate practices. They are soft law instruments, and as such do not give rise to legally binding obligations. As a result, **despite the beneficial influence of the UNGPs and the OECD Guidance and the existence of numerous initiatives such as industry schemes and standards**, the actual **implementation of due diligence guidance for human rights and environmental impacts by businesses has been insufficient** in practice. As shown in detail in Section 2.2.2.3/Annex 10 of the Impact Assessment, over the past decade, voluntary due diligence standards have not been effective in mainstreaming adequate impact management.[[312]](#footnote-313) The majority of businesses still do not carry out due diligence and many of those who do, do not do so in a way that is effective or in line with international standards.[[313]](#footnote-314) While frontrunners are integrating sustainability into their business models, transition is too slow.[[314]](#footnote-315) As a result of voluntary measures failing to generate meaningful change in the way companies manage their negative impacts, forced labour, inadequate workplace health and safety, environmental damage, etc. continue to arise.[[315]](#footnote-316) Moreover, it is difficult for frontrunners to take further steps forward without support from the regulator due to short-term pressure.

Stakeholders recognize the limitations of the voluntary framework. Survey respondents in the Supporting study on due diligence did not express support for EU horizontal guidance on due diligence for sustainability impacts. They considered that there is already enough voluntary guidance and that new voluntary guidance alone would not have notable social, environmental and human rights impacts.[[316]](#footnote-317) Equally, respondents to the public consultation agreed that voluntary approaches and reporting cannot bring about the necessary behavioural change and have expressed a clear support for a mandatory approach.[[317]](#footnote-318) Nevertheless, businesses[[318]](#footnote-319) expressed some hesitation when it comes to the need for action on an EU framework for due diligence and suggested further developing and supporting voluntary schemes. They expressed concern about administrative burden for companies already facing difficulties due to the COVID-19 crisis, the inability to fully identify the supply chain, and perceived loss of competitiveness of EU companies, while doubting the potential of legally binding rules to cease negative impacts. They therefore urge to focus on exploiting and strengthening the role of States and the EU’s foreign, security and development policies with a view to mitigating adverse impacts locally.

At the same time, a recent report of the UN Special Rapporteur on extreme poverty and human rights warned against an overreliance on voluntary, private sector efforts.[[319]](#footnote-320) The UN Working Group on Business and Human Rights has stressed in a recent publication marking the 10-year anniversary of the UNGPs that “[t]*he last decade has underscored the point made in the UNGPs: voluntary approaches alone are not enough. The rise of mandatory measures will undoubtedly accelerate both uptake and progress*”.[[320]](#footnote-321)

As a matter of fact, **the EU has already gone beyond such guidance and a voluntary approach with imposing sustainability reporting obligations on companies under the scope of the NFRD**, and henceforth under the scope of the new CSRD, thereby fostering due diligence practices through reporting. In addition to the Supporting study on due diligence, other studies[[321]](#footnote-322) have also shown that the impact of existing reporting requirements on corporate practices have remained limited to date: they are interpreted as focusing on material risks to the company and do not sufficiently take into account the impact of the company’s activities on people and planet. Moreover, they only impose an obligation to report and not an obligation to prevent and mitigate risks and thus they only regulate one element of the 5-step due diligence process recommended by the existing international voluntary frameworks. While the CSRD is expected to improve corporate reporting, the above-mentioned study revealed that reporting alone is not sufficient to mainstream responsible behaviour. **Although the NFRD had some positive impact[[322]](#footnote-323),** only a third of companies carry out fully fledged due diligence, despite the reporting requirement already in place. **Due to the proven inefficiency of a reporting approach to mainstream proper risk and impact management and responsible corporate behaviour**, it is **unlikely that a reporting requirement – even if improved by CSRD proposal – will bring about the necessary changes in the future.**

Furthermore, EU guidance addressed to companies or a recommendation addressed to Member States would not resolve, and could even **exacerbate, legal uncertainties** as regards what the duties of companies are and what they are liable for. Finally, an EU recommendation may result in some Member States not taking any action or only limited action, thereby creating **further disparities, fragmentation, costs and burden for companies**.

### Civil liability not regulated

In the options screening phase, a potential policy option covering a mandatory due diligence requirement without a civil liability regime has been considered.

While administrative supervision alone could in theory ensure enforcement to prevent and mitigate the risk to harm, the 2016 implementation report of the EU Timber regulation[[323]](#footnote-324) – the only EU law containing a sector specific due diligence obligation which has been applicable for some time – shows that **effective enforcement through administrative supervision remains a major challenge**. On the other hand, the French law based on civil liability appears to have been effective in fostering compliance[[324]](#footnote-325).

Civil liability is **therefore necessary to provide for a proper enforcement regime for the duty to prevent and mitigate harm, in addition to administrative enforcement.**

As the UN Human Rights Office of the High Commissioner states[[325]](#footnote-326), it is necessary to ensure that the design of the due diligence regime is capable, in practice, of delivering on the key aim of strengthening due diligence by companies so as to prevent and address business-related harms.

Second, under the voluntary framework, there is **currently legal uncertainty about how far companies are liable** for their failure to address human rights and environmental adverse impacts occurring in their value chains, and **emerging law and jurisprudence is incoherent among Member States**.

Emerging jurisprudence confirms the liability of companies for failing to mitigate harms e.g. greenhouse gas emissions in their own operations, in the group and within business relationships: mitigation of such harm is part of a company’s standard of care vis-à-vis others and the society, the breach of which needs to be repaired.[[326]](#footnote-327) National law (i.e. the French duty of vigilance law) or law in the making (Dutch Bill on Responsible and Sustainable International Business Conduct, Austrian Parliamentary Proposal for a supply chain law,, Belgian Parliamentary Vigilance Proposal)[[327]](#footnote-328) also include liability provisions, albeit different. With a view to providing legal certainty around the extent of the liability linked to the due diligence duty and ensuring a level playing field for companies in the single market, civil liability provisions are necessary. **However,** **in line with subsidiarity, only those aspects of civil liability would be regulated** which are necessary for providing such legal certainty(e.g.limitation periods, burden of proof, etc. would not be regulated).

Furthermore, civil liability is important to ensure that victims of adverse impacts can get **access to remedy**. International voluntary standards, such as the UNGPs already expect companies to remedy such harm.[[328]](#footnote-329) Mandatory due diligence with a civil liability element, and conditions when such liability applies, would help improve **access to justice for victims** of corporate adverse impact in third countries. Victims of corporate human rights and environmental harms currently face well-documented barriers to access remedies against companies.[[329]](#footnote-330) An enforcement regime that only comprises administrative supervision, even if combined with elements of taking the company’s remedial actions into account, does not provide for access to remedies for those affected by the harms. Many stakeholders participating in the open public consultation and in the survey in the context of the supporting study on due diligence, especially those from civil society and trade unions, consider access to remedy to be an essential part of a regulatory option.[[330]](#footnote-331)

In the survey conducted in the context of the Due Diligence Study, some interviewees from multinational companies did not agree with the views of other stakeholder groups, including other businesses regarding liability regimes and methods of enforcement.[[331]](#footnote-332) Some business respondents to the open public consultation argued that civil liability is undesirable given the varying liability regimes across the Member States. This approach would potentially lead to forum shopping.[[332]](#footnote-333) These respondents argued that civil liability could lead to a wave of lawsuits and negative publicity for companies. They consider that, if companies fear that they may be held legally liable for any human rights harm anywhere within their value chains, irrespective of the circumstances of their involvement, they could consequently be discouraged to carry out business in 'risk areas' that might however depend heavily on such business activities to survive. According to businesses respondents, there is a need to acknowledge companies’ efforts and protect them against lawsuits, otherwise they will disengage from risky markets.[[333]](#footnote-334)

As regards such arguments, first of all, the experience with the French Vigilance law – to be seen in the context of the scope of that legislation obviously – so far has not brought about a wave of lawsuits.[[334]](#footnote-335)

As regards forum shopping, the aim is to regulate civil liability to an extent which would provide for legal certainty and level playing field in the required standard of conduct, this limits the risk of forum shopping.

The concern that a civil liability would prompt businesses to disengage from risky markets is not warranted. On the one hand, the risk of disengagement from some markets is not linked to liability per se but to the compliance with the duty: i.e. if some markets are considered too risky, the company may decide not to buy from those regions (if other alternatives are available), irrespective of the threat of liability. Conducting proper due diligence will actually enable companies to manage better their liability risk and a harmonised liability regime will facilitate that.

In addition, **liability will be adapted to what can reasonably be expected from companies, in particular with respect to their value chains**. Under all policy options, only foreseeable risks may trigger liability. The commentary on Principle 18 of the UNGPs state that the purpose of human rights impact assessments, as an element of due diligence, is to ‘understand the specific impacts on specific people, given a specific context of operations’. Liability will therefore be linked to risks of adverse impacts to reasonably foreseeable classes of victims, for reasonably foreseeable classes of adverse impacts. This will include risks that the company was informed about. Furthermore, there will be no liability when identifying and/or addressing adverse impacts occurring beyond direct contractors would prove to be unsuccessful despite the company’s reasonable efforts. Such reasonable efforts could include requesting suppliers through contractual clauses to ensure the cascading of the obligations, or preventing the harm, where necessary, through cooperation with other companies and engaging in industrial schemes or by using financial means. Furthermore, the buyer company will not be made liable for wrongful action of their supply chain partners. It will be liable for the consequences of its own failure to exercise proper due diligence, with regard to the enterprises over which they have control or effective leverage or over which they could have exercised leverage through reasonable efforts as mentioned above.

### Regulatory measures with due diligence obligation stopping at direct (tier-one) suppliers

Options in which the **due diligence obligation** would be **limited to the company’s direct suppliers (so-called first-tier supplier)** have not been selected, for several reasons.

First, the **most relevant adverse impacts on human rights and on the environment occur** mainly outside the EU. They are typically beyond direct suppliers, **further upstream in the value chain**, for instance at the stage of raw material sourcing and at initial manufacturing stages[[335]](#footnote-336). Furthermore, they may take place **in the downstream value chain**[[336]](#footnote-337) or **would be linked to the impact of the product itself**[[337]](#footnote-338).

Second, the due diligence obligation should build on **recognised existing international voluntary standards** and these **expect companies to undertake due diligence in their entire value chain**.[[338]](#footnote-339) For example the UNGPs state that human rights due diligence “should cover adverse human rights impacts that the business enterprise may cause or contribute to through its own activities, or which may be directly linked to its operations, products or services by its business relationships”. The OECD MNE guidelines also cover situations where the company not only causes or contributes to but is directly linked with the adverse impact. “Linkage” is defined by the relationship between the adverse impact and the enterprise’s products, services or operations through another entity (i.e. business relationship). “Directly linked” is not defined by direct contractual relationships, for example “direct sourcing”[[339]](#footnote-340). Jurisprudence interpreting the voluntary framework, such as the Shell judgement also require focus on the entire value chain, including the use phase. Closely related horizontal EU instruments (such as the NFRD, CSRD proposal or the taxonomy regulation) apply to the entire value chain, including the use phase.

Third, **companies have in most cases tools** at their disposal to create visibility and **exert leverage** over their value chain even beyond direct suppliers, and under the existing international frameworks it is expected that the buyer uses leverage over suppliers beyond tier one. Such recommended action include the use of (cascading) contracts, concluding direct contracts with the supply chain member which is not direct contractor, cooperation with another company which is direct contractor of that value chain member to exert common pressure, financial or other support, etc.[[340]](#footnote-341) Control can also be exercised over the impact of the product[[341]](#footnote-342).

Lastly, an obligation covering only parts of a company’s value chain is **easily circumvented** by artificially establishing entities in the value chain to avoid compliance.

In conclusion, limiting companies’ due diligence obligation to the first tier of their value chains would seriously compromise the effectiveness of this initiative and jeopardise its purpose. Therefore, in the options assessed in detail the due diligence obligation will not stop at harm occurring at the level of direct suppliers but the company will only be liable for harm beyond the level of direct business relationships if it did not complete certain reasonable steps.

### Regulatory measures with enforcement through civil liability limited to direct (i.e. tier-one) suppliers

Limiting civil liability to harm caused at the level of the direct supplier is another regulatory option that has been considered when screening potential policy options. It has been discarded for the following reasons.

As explained above, most adverse human rights and environmental impacts take place beyond direct suppliers and existing international frameworks already now expect companies to address these impacts. As the planned due diligence obligation will **build on existing international frameworks**, it will capture harms beyond direct suppliers and will require using leverage where the company can do so though reasonable efforts. **Limiting liability to adverse impact at the level of tier-one suppliers only would be more limited than what the company is expected to, and is able to do** to address harm in practice. Such a liability regime would therefore not mirror the due diligence obligation. As explained above, liability will be significantly limited beyond tier-one suppliers.

Consequently, limiting the liability strictly to tier one and thus departing from the approach of existing voluntary frameworks would create considerable **legal uncertainty**. This would be particularly counterproductive in light of **emerging jurisprudence** establishing such liability beyond tier-one suppliers (such as the recent Shell judgement) and jeopardising the impact of such jurisprudence.

# Description of policy options retained for detailed assessment

All regulatory options include a due diligence obligation for companies. The four packages of regulatory options that were retained for a detailed assessment differ from each other in terms of the **personal scope of application** and **the content** of the corporate due diligence obligation. The following sections explains these differences, as well as the **elements that are common to all policy options** assessed in detail.

### Personal scope

The policy options assessed in detail differ from each other in terms of the **size** of the companies covered by the scope. In addition, they either include all (non-micro sized) **listed** companies (companies that have securities admitted to trading on a regulated market,) or not, and they either apply to all sectors of the economy **horizontally** or are limited to companies that are active in **specific sectors** or pursue specific economic activities. The options assessed also combine the size criterion with the sectoral approach (and with other criteria related to the content of the due diligence obligation).

#### Company size categories covered

While the basis of defining the various size categories for identifying and assessing the options that are retained for detailed assessment is the Accounting Directive[[342]](#footnote-343), we use these definitions only for listed companies and where the scope is aligned with that of the CSRD proposal. Otherwise we use **slightly amended (simplified) definitions for medium-sized and large companies** (based on the number of employees and/or the turnover). We also introduce **additional categories** of larger companies: three variants for defining **very large companies** and two middle-ground categories of large companiesto differentiate **midcaps** from the very large companies.

To avoid undue administrative and financial burden for small companies, **both micro-enterprises and small companies** are excluded from the scope of all options analysed in detail, except for small (but not micro) listed companies which are covered by two options. Still, some of the smaller companies excluded from the scope will nevertheless be **indirectly** impacted as part of the value chain of companies in the scope due to a **trickle-down effect**, i.e. when the larger EU company implements its due diligence obligation and asks its supply chain to comply with its sustainability requirements.

Due diligence requirements will also apply to **large companies without an EU establishment** but operating in the EU and having generated a significant turnover in the EU. The imposition of due diligence obligations on third-country companies is in line with applicable jurisprudence, provided that there is a connecting factor with the EU territory (principle from the Lotus Case, PCIJ, 1927). In this case, the connecting factor would be the turnover made in the EU. The relevant threshold will therefore need to be selected to constitute an adequate turnover that sufficiently connects to the EU territory having also regard to the option eventually selected for EU companies.

#### Sectors covered

The options include sectoral and horizontal approaches as well a combination of these. In the combined options, large (or very large companies, depending on the option) will be subject to the full due diligence duty, while medium-sized (and midcaps, depending on the option) which operate in high-impact sectors and which are not value chain partners or subsidiaries of those larger companies will have to comply only with a targeted duty.

Such high-impact sectors would need to be identified based on specific criteria, and with possibility to regularly review this as necessary. Criteria to select the sectors should build on existing EU law defining high impact sectors for climate change impacts, including as regards value chain impacts, other relevant EU work regarding other environmental impacts and existing national sector lists for human rights impacts, as well as sectors defined in OECD due diligence guidance.

For the purposes of the impact assessment, an indicative “maximum” list as well as more limited list of possible high-impact sectors and subsectors is provided in Annex 11. These were selected on the basis of the EU ETS, the EU Benchmark Regulation, national lists of risky sectors from a human rights perspective and other criteria, as explained in that Annex.

### Content of the due diligence obligation

The policy options that have been retained for detailed analysis also vary depending on the **impact categories** covered (theme-specific or horizontal) and, as explained above, the **extent** to which the specific categories of companies have to fulfil the due diligence obligation (focus on all risks or most relevant risks only).

The **thematic or theme-based approach** covers only certain impact types (similarly to the Dutch child labour act). Such rules could be adopted only for a limited number of themes, for example climate change, forced labour, child labour, or other human rights, including labour rights impacts, biodiversity, pollution. The due diligence obligation would not be limited then to certain pre-selected sectors but would apply to all companies which are concerned by these impact types.

Regarding impact categories, part of the options include a due diligence obligation that extends to **all** human rights and environmental impacts in a comprehensive manner.

**Human rights impacts** are understood as the violation of human rights contained in international human rights conventions listed in Annex 17[[343]](#footnote-344).

**Environmental impacts** are those specified in selected international environmental conventions which contain duties that are implementable for companies, such as those listed in Annex 17[[344]](#footnote-345).

Concerning greenhouse gas emissions` mitigation, companies should set and disclose a target which gives an indication of their plans on how to comply with the impact mitigation duty. [[345]](#footnote-346), [[346]](#footnote-347)

Meeting **the target will not be a legally binding obligation and thus not lead to a proof of non-compliance or liability under the due diligence obligation**. Specific circumstances may justify the company’s deviation from its own target or makes compliance with it difficult.

Some of the options assessed (also) contain a **targeted (simplified) due diligence obligation** which requires companies to identify, prevent and mitigate only their **most relevant** adverse human rights and environmental impacts. This is **combined with the sectoral approach and with the differentiation according to company sizes**, as a result of which “smaller” companies operating in selected, high-impact sectors would only need to focus on their most relevant impacts. For example, a chocolate company (above a certain size) could be expected to focus on: right to life, forced labour, child labour, climate change, biodiversity; a textile company would be expected to focus on forced labour, health and safety, living wage, pollution, climate change; a chemicals company would be expected to focus on pollution through discharge of chemicals, biodiversity, climate change, health and safety, forced labour. **Such most relevant**  **impacts in a given sector** will need to be identified for the targeted due diligence, building on the existing OECD sectorial guidance, and taking into account the work on the CSRD reporting framework which focuses on identifying issues relevant for determining sector-specific impacts.

### Enforcement

All option packages include both civil liability and administrative enforcement, which operate in a complementary manner.

#### Administrative supervision

Member States would be required to **appoint a national administrative supervisory authority** to supervise compliance with the new obligations. They would be allowed to appoint more than one authority if necessary. The supervisory authority would be required to **supervise companies *ex officio*** and to conduct investigations **based on complaints**. Complaints will be allowed to be filed with the competent national authority, such as from affected persons.

The authority should have the power to **investigate** non-compliance and impose **sanctions**. The sanction regime will be such that is also effective against third-country companies whilst not discriminating between third-country and EU companies.

As administrative fines could be difficult to enforce vis-à-vis third-country companies, they may not have sufficient deterrent effect on them. Therefore, the legal proposal could include a non-exhaustive list of other sanctions (applicable to both EU and the covered non-EU companies) to reinforce the effectiveness of the regime and ensure level playing field between EU and third-country operators.

Such sanctions could include: a public “naming and shaming” statement, indicating the nature of the infringement, or banning from public procurement In case of serious adverse impacts, such as (but not limited to, and thereby not differentiating between similarly egregious abuses) forced labour, the supervisory authority could also order the withdrawal of products from the market linked to serious adverse impacts.

Such a sanction regime could effectively contribute to fostering more sustainable practices, including by third-country companies.

An **EU system of cooperation between the national competent authorities** would be set up. EU supervisors would be required to exchange information and provide mutual assistance. Such a system would facilitate investigations, implementation of sanctions, cooperation to ensure coherence in sanction and the level of fines, etc.

For the purposes of effective supervision, the third-country company would be required to **appoint an authorised representative**.[[347]](#footnote-348) With a view to ensure that the third-country company is not discriminated against compared to EU businesses, the legislation will clearly define the obligations of the representative.

In case a national supervisory authority orders the temporary suspension of activities in that Member State, national supervisory authorities cooperating under the EU supervisory cooperation mechanism could decide to extend that sanction to their territories as well.

#### Civil liability

Civil liability for a failure to carry out due diligence would be introduced, similarly to the French law.

The company would be liable for damages if (i) the company did not comply with its due diligence obligation (i.e. the obligation to prevent or mitigate harm in its own operations, in its subsidiaries, in the value chain or with respect to the impacts of its products and services), including when it did not carry out due diligence measures adequately, (ii) where the harm was foreseeable, and (iii) the harm could have been prevented by proper due diligence measures. The condition that only foreseeable risks can trigger liability is in line with the general principles of tort law.

More specifically, the company will be liable for the harm that could have been prevented or mitigated in their own operation and its subsidiaries where the company has “ownership control”, and at the level of direct suppliers/relationships where the company has “control through contract or financing”. However, the lead company will not be liable beyond direct suppliers unless it did not take every reasonable step to prevent/mitigate the harm, for example by requesting its suppliers through contractual clauses to ensure the cascading of the obligations, and taking action to ensure that cascading of obligations will be practiced, or mitigating the harm, where necessary, through engaging in collaborative industrial schemes or by using financial means (considered as ‘reasonable steps’). The company’s liability will not cover harm occurring at the level of one-off suppliers beyond tier one.

### Other elements common to all options

In addition to limiting the personal scope of application and the content of the due diligence obligation in different combinations to ensure proportionality, each option will be combined with elements **to limit the possibility of passing on the entire compliance burden to supply chain partners, in particular to SMEs**[[348]](#footnote-349).

Furthermore, the legislative initiative will be **accompanied by other support measures** in order to limit the burden on the companies and help them with the implementation. These could include, for instance, sectorial guidelines and online tools that could be adopted by Member States; a helpdesk at national level, promotion and facilitating the creation of industrial alliances, technology support for data sharing solutions, technology solutions for tracing the value chain, capacity building as well as additional supporting measures in third countries.

The due diligence process includes communicating on adverse impacts and how adverse impacts are addressed. This reporting will be covered by the Corporate Sustainable Reporting Directive for all companies within its scope. Under the CSRD, reporting standards will be developed. For medium-sized companies not covered by the CSRD (above 50 employees), the corporate governance initiative will require reporting duties building also on the ongoing work of the European Financial Reporting Advisory Group (EFRAG) task force working on reporting standards, including sector specific ones.

### Option 1: Sector or theme-specific mandatory due diligence for all large and high-impact medium-sized companies

This option would introduce sector- or theme-specific mandatory due diligence.

A **sector-specific** measure could apply to one or more selected sectors. In the latter case, it would apply to a limited number of sectors that are exposed to adverse human rights and environmental impacts, such as minerals, construction, chemicals, garment and footwear, manufacturing of consumer goods, rather than applying to a more refined list of high-impact sectors, subsectors and economic activities, such as the indicative list in Annex 11.

Sectoral rules would apply to all **large companies** and **all medium-sized companies** as well as **all listed (i.e. including small other than micro) companies** in the specific sector(s). They would also apply to **third-country** companies with an EU turnover of at least EUR 350 million if they operate in the given sector(s).

Depending on the sector, the human rights and environmental impacts covered in due diligence could be limited to the **most important risks** in that sector (similarly to the Conflict Minerals Regulation) **or** it could apply to **all types of impacts**. As in all other options assessed in detail, harm in the company’s own operations, in subsidiaries, in its value chains as well as impacts linked to its products and services would be covered.

|  |  |  |
| --- | --- | --- |
| **Option 1a:** | | |
| **Company category**  **(EU LLCs)** | **Definition** | **No. of EU LLCs covered:[[349]](#footnote-350)** |
| **Large (simplified def.)** | employees > 50 AND turnover > EUR 8 million, excluding medium-sized companies (simplified def.), in the selected sector(s) | depending on the sector(s) |
| **Listed non-micro SMEs** | as defined in Accounting Directive, in the selected sector(s) | same |
| **Non-listed medium-sized (simpl. def.)** | 50 < employees ≤ 250 AND 8 m < turnover ≤ 40 m (EUR), excluding listed medium-sized, in the selected sector(s) | same |

Alternatively, as explained under the general description of the options above, **theme-specific** rules could be adopted for some impact types, for example climate change, forced labour, child labour, and other human rights, including labour rights, biodiversity, pollution. Such a measure would cover the same sized companies as the sectoral approach with regard to the specific issue. Given the limited data on the turnover of third country companies, it is not possible to estimate the number of those companies falling in the scope of this initiative under any of the options described.

|  |  |  |
| --- | --- | --- |
| **Option 1b: theme specific** | | |
| **Company category**  **(EU LLCs)** | **Definition** | **No. of EU LLCs under very targeted DD:[[350]](#footnote-351)** |
| **Large** | employees > 50 AND turnover > EUR 8 million, excluding medium-sized (50 < employees ≤ 250 AND 8 m < turnover ≤ 40 m (EUR)), in all sectors | 24 120 |
| **Listed non-micro SMEs** | as defined in Accounting Directive, in all sectors | 1 410 |
| **Non-listed medium-sized (simpl. def.) in high-impact sectors** | 50 < employees ≤ 250 AND 8 m < turnover ≤ 40 m (EUR) in high-impact sectors (70%), excluding listed medium-sized in high-impact sectors | 19 880 |

This option would also include **measures to support** companies, in particular SMEs[[351]](#footnote-352). including those that are not directly in the scope but are nevertheless affected by the measure because they are a direct or indirect supplier of a company that is required to comply with the due diligence obligation. Option 1 also comprises elements to limit the passing on of all compliance burdens to the smaller companies in the supply chain.

Regarding enforcement, this option would include administrative supervision and harmonised civil liability rules, in line with the approach explained above. In addition, rules overriding conflicting private international law as regards applicable law would be adopted to facilitate access to remedy for victims of harm.

### Option 2: Horizontal mandatory full due diligence applying to very large companies

Unlike Option 1, this option would introduce a due diligence obligation applying to companies **across industry sectors**. The obligation would cover **all human rights and environmental impacts** and the company would be required to conduct full due diligence including in its own operations, in subsidiaries, and through its value chain.

Option 2 would apply only to **very large** limited liability companies that have at least 1000 employees. It will also apply to **third-country** companies with an EU turnover of at least EUR 350 million.

|  |  |  |
| --- | --- | --- |
| **Option 2:** | | |
| **Company category**  **(EU LLCs)** | **Definition** | **No. of EU LLCs under full DD:[[352]](#footnote-353)** |
| **Very large (var. 1)** | Companies with > 1000 employees in all sectors | 8 910 |

Similarly to option 1, option 2 would include measures to support companies, including in particular SMEs[[353]](#footnote-354) that are not directly in the scope but are nevertheless affected by the measure because they are a direct or indirect supplier of a company that is required to comply with the due diligence obligation. Option 2 also comprises elements to limit the excessive passing on of all compliance burdens to the smaller companies in the supply chain.

Furthermore, this option would also include administrative supervision and harmonised civil liability rules, as explained above. This option will also include rules overriding conflicting private international law as regards applicable law to facilitate access to remedy for victims of harm.

### Option 3: Horizontal full due diligence obligation applying to very large companies, targeted due diligence for midcaps and medium-sized companies

Like Option 2, this option would establish a due diligence obligation that is **horizontal**, i.e., applying across industry sectors. **Very** **large companies** (a) with over 500 employees or with a turnover exceeding EUR 350 million (approximately 23 300 EU companies) or (b) with over 500 employees and with a turnover exceeding EUR 150 million (about 9 400 EU companies) would be required to comply with the **full** due diligence duty covering all types of risks. It will also apply to **third-country companies** with an EU turnover of at least EUR 350 million.

**Midcaps and medium-sized companies** (i.e. (a) LLCs with 50 to 500 employees and a turnover of EUR 8 to 350 million or (b) LLCs not exceeding both the 500 employee and the EUR 150 million turnover but having at least 50 employees and a turnover above EUR 8 million) would be subject to a **targeted due diligence obligation** insofar as they are active in one of the **high-impact sectors** identified on the basis of specific criteria and listed in a delegated act. As explained earlier, an indicative “maximum” list and more limited lists of possible high-impact sectors are included in Annex 11. However, in case they are a subsidiary or value chain partners of larger companies, they will most likely have to perform more broader due diligence.

These companies would have to identify, prevent and mitigate their **most relevant** adverse human rights and environmental impacts. This will depend on the sectors they operate in and will be identified, taking also into account the sector specific disclosure framework which is being developed by the EFRAG taskforce on sustainability reporting standards.[[354]](#footnote-355) Due diligence obligations for such companies would be **phased-in** at a later stage.

|  |  |  |  |
| --- | --- | --- | --- |
| **Option 3a:** | | | |
| **Company category**  **(EU LLCs)** | **Definition** | **No. of EU LLCs under full DD** | **Maximum no. of EU LLCs under targeted DD[[355]](#footnote-356)** |
| **Very large (var. 2)** | employees ≥ 500 OR turnover ≥ EUR 350 million in all sectors | 23 290 |  |
| **Midcaps in high-impact sectors** | 50 < employees ≤ 500 AND 8 m < turnover < 350 m (EUR) in high-impact sectors, excluding medium-sized in high-impact sectors (70%)\* |  | 12 590 |
| **Medium-sized in high-impact sectors** | 50 < employees ≤ 250 AND 8 m < turnover ≤ 40 m (EUR) in high-impact sectors (70%)\* |  | 20 110 |
| **Total number of companies covered:** | | 55 990 | |

\**Correcting for being part of the groupº of larger companies that fall under a full due diligence obligation and therefore indirectly impacted by full obligation, as explained in Annex 11.*

|  |  |  |  |
| --- | --- | --- | --- |
| **Option 3b:** | | | |
| **Company category**  **(EU LLCs)** | **Definition** | **No. of EU LLCs under full DD** | **Maximum no. of EU LLCs under targeted DD[[356]](#footnote-357)** |
| **Very large (var. 3)** | employees ≥ 500 AND turnover ≥ EUR 150 million in all sectors | 9 360 |  |
| **Midcaps in high-impact sectors** | employees > 50 OR turnover > EUR 8 million in high-impact sectors, excluding medium-sized (simplified definition) in high-impact sectors and  very large LLC in high-impact sectors (70%)\* |  | 14 530 |
| **Medium-sized in high-impact sectors** | 50 < employees ≤ 250 AND 8 m < turnover ≤ 40 m (EUR) in high-impact sectors (70%)\* |  | 20 110 |
| **Total number of companies covered:** | | 44 000 | |

\**Correcting for being part of the group of larger companies that fall under a full due diligence obligation, as explained above and in Annex 11.*

Like Options 1 and 2, this option would provide for administrative supervision and harmonised civil liability rules. This option will include rules overriding conflicting private international law as regards applicable law to facilitate access to remedy for victims of harm by the due diligence law.

Option 3 would also put in place provisions to support companies and also to limit the passing on of all compliance burdens to the smaller companies in supply chain.

### Option 4: Scope of horizontal full due diligence obligation aligned with CSRD (large companies and listed companies) and targeted due diligence obligation applying to non-listed medium-sized companies

Like Options 2 and 3, this option would require companies across **all industry sectors** to carry out due diligence. The obligation would cover **all human rights and environmental impacts** and the company would be required to identify and mitigate adverse impacts in its own operations, in subsidiaries, through its value chain as well as impacts linked to its products and services.

Option 4 would have the **widest personal scope** of all options, covering more or less 80 000 EU companies. All **large** companies (as defined in the Accounting Directive, i.e. exceeding 2 out of the 3 thresholds: 250 employees, a turnover EUR 40 million turnover, EUR 20 million balance sheet total) as well as all **listed** companies (except for micro enterprises) would be required to carry out **full** due diligence. In addition, other (non-listed) **high-impact medium-sized** companies (defined as having 50 to 250 employees and a turnover between EUR 8 and 40 million, and active in the selected high-impact sectors) would be required to carry out **targeted due diligence**. Like under Option 3, calculating with the indicative list of such sectors, maximum 19 880 EU medium-sized companies would be covered by the targeted duty. This option will also apply to **third-country companies** with an EU turnover of at least EUR 350 million.

|  |  |  |  |
| --- | --- | --- | --- |
| **Option 4:** | | | |
| **Company category**  **(EU LLCs)** | **Definition** | **No. of EU LLCs under full DD** | **Maximum no . of EU LLCs under targeted DD[[357]](#footnote-358)** |
| **Large** (as under the scope of the CSRD**)** | as defined by the Accounting Directive, in all sectors | 65 040 |  |
| **Listed non-micro SMEs** (as under the scope of the CSRD**)** | as defined in Accounting Directive, in all sectors (out of which listed medium-sized in high-impact sectors: 230) | 1 410 |  |
| **Non-listed medium-sized (simpl. def.) in high-impact sectors** | 50 < employees ≤ 250 AND 8 m < turnover ≤ 40 m (EUR) in high-impact sectors (70%), excluding listed medium-sized in high-impact sectors) |  | 19 880 |
| **Total number of companies covered:** | | 86 330 | |

The enforcement regime would be the same as under other options, including both administrative supervision and harmonised civil liability, as explained above. This option will also include rules overriding conflicting private international law as regards applicable law to facilitate access to remedy for victims of harm.

Option 4 would include provisions to support companies and also to limit the passing on of all compliance burdens to the smaller companies in supply chain.

# Options for directors’ duties

## Discarded options: non regulatory measures and regulating directors’ duties in Corporate Governance Codes through recommendation

Non-legislative options in the area of directors’ duties could include **enhancing voluntary steps by non-regulatory measures or soft EU law instruments** such as Commission-led or EU-funded awareness-raising campaigns and trainings for directors, Commission Guidelines for directors, or a Commission Recommendation for Member States to adjust the Corporate Governance Codes or to clarify their national laws.

As the Non-financial Reporting Directive already requires disclosure on sustainability risks and their management by certain large companies, and evidence shows that mandatory reporting was not sufficient to mainstream good practices to a satisfactory level, the effectiveness of non-legally binding intervention in addressing the problems is likely to be limited despite the enlarged scope of the revised Non-financial Reporting Directive. The consultation activities show support for regulatory intervention rather than for soft law, but also reveal differences in the views of businesses[[358]](#footnote-359).

Against this background, the **clarification of the general duty for directors to act in the interest of the company in** **Corporate Governance Codes** was assessed in more detail as it had been suggested as an appropriate way forward by certain stakeholders. In the end, this option, similarly to other purely non-legally binding EU solutions, was discarded for several reasons.

First of all, such Codes apply only to listed companies, and often only to a limited scope among them (top segment of the stock exchange), while the problems identified are more far-reaching and short-termism has a systemic character.

Secondly, even if all Codes would be adjusted to reflect on a possible EU Recommendation, the Codes themselves are not legally binding and apply only on a “comply or explain” basis. Therefore, Codes are unlikely to generate and mainstream the paradigm shift necessary to attain the identified objectives. It has to be noted that previous EU recommendations which recommended Member States to introduce new corporate governance requirements for example on directors’ remuneration have been found ineffective and were subsequently made mandatory through the revisions of the Shareholders Rights Directive.

Also, national law regulating the directors’ duty of care and duty to act in the interest of the company applies generally to all limited liability companies, and possibly even beyond them to all business undertakings, which makes the amendment of the legislative rules – in harmonised manner across the EU – a legally more sound solution.

Furthermore, amending the Codes would not solve the problem of legal uncertainty, in particular in Member States where there is no jurisprudence emerging from national courts regarding proper consideration of stakeholder interests and longer term implications within the company interest. As the problems to be addressed are, at least partially, rooted in the lack of clarity of national company laws, a soft law measure is not likely to bring about a harmonised interpretation across all Member States, including by the courts, and to counter the identified EU-wide market failures. Further discrepancies will also result in unnecessary costs and burden.

Finally, legal rules on sustainability risk management are in the pipeline for example through the ongoing revision of the banking rules (CRD and CRR) and other measures announced in the revised Sustainable Finance Strategy. The risks of the financial sector and non-financial companies are interrelated and the approach to regulate such risks and their management should be coherent.

Accordingly, purely non-legally binding EU solutions as well as changes to corporate governance codes were discarded.

## Description of the directors’ duties concerned

This section provides a detailed description of the general and the specific duties of company directors addressed by this initiative.

***I. Clarification of the directors’ general duty to act in the interest of the company***

It should be clarified that directors of limited liability companies, when acting in the best interest of the company, should take into account the **likely medium and long-term consequences** of their decisions and resolutions, and should also duly take into account the **interests of the company’s stakeholders**, including in particular its members or shareholders, creditors, employees (including employees in the supply chain), customers, suppliers, the local communities[[359]](#footnote-360) and other groups of people, communities and entities that are or can be affected by the company and its value chain. They will also have to take into account the interests of the local and global environment (including the climate)[[360]](#footnote-361).

***II. Specific duties for directors***

*Risk management and setting up and overseeing corporate risk management systems*

In order to comply with the general duty to act in the best interest of the company, directors should identify the company’s key stakeholders and the interests of those stakeholders. They should manage the risks to the company linked to such interests, the company’s dependencies linked to these stakeholders (including the environment) and risks arising from the company’s impacts on its stakeholders (including environmental impacts). Directors should identify and manage such risks in the short, medium and long term and such risk management should also extend to the group (where relevant) and to the value chain.

*Impact management: Setting up and overseeing the implementation of corporate due diligence processes and measures (incl. impact identification and assessment, tracking effectiveness and reporting policies, procedures and prevention measures)*

Where the company is obliged to carry out due diligence through its value chains with regard to environmental harm and human rights violations, the directors should be responsible for setting up and overseeing the policies, processes (systems, functions, procedures) and measures necessary to comply with the duty.

*Incorporating stakeholders’ interest and sustainability aspects (risks, opportunities, impacts) in the corporate strategy*

In order to reach the objectives of this initiative, it is important that sustainability matters are properly dealt with at the highest level of corporate decision-making and that the corporate strategy and business model is compatible with proper sustainability risk and impact management. Directors should therefore ensure that the corporate strategy properly takes into account the short-, medium and long-term interests of stakeholders and other sustainability aspects, and in particular that it integrates the prevention of the company’s adverse impacts in compliance with the company’s due diligence obligation.

Directors of some companies (depending on the options) should adopt and implement, as part of their corporate strategy, a science-based target for climate change mitigation[[361]](#footnote-362).

A science-based target would be defied as follows: (1) one which is in line with the maximum of 1.5 degrees global warming objective compared to pre-industrial levels based on the latest scientific knowledge (2) which covers all greenhouse gases (3) which includes short-term, medium and long-term targets quantifiable in absolute reduction levels compared to the base year, (4) which, if relevant, takes into account applicable national targets and other law (6) the use of carbon capture and storage processes to compensate for emissions would be allowed.[[362]](#footnote-363)

To ensure that such a target becomes strategic and is properly implemented, decision makers at highest level in the company should play a role in their adoption and implementation. Such targets could also be foreseen for biodiversity, however the adoption of the post 2020 Biodiversity Convention is planned for early 2022 only. Such a target is therefore subject to the adoptions of the international framework in this field and could be added when such framework is adopted.

*Engagement with stakeholders*

Directors should establish a proper form for **regularly engaging with stakeholders, i.e.** employees’ representatives and other major stakeholder groups (such as suppliers, other entities and local communities along the value chains) and relevant non-governmental organisations representing the interests of the environment, for example. Beyond the consultations related to adverse impact identification and mitigation as explained in the section on due diligence, engagement can take the form of establishing an advisory group, conducting regular consultations without establishing a formal structure for such consultations, including using existing consultation channels, such as for example with employees.

Meaningful engagement with the relevant stakeholders can help directors act in the interest of the company, set the right strategy, manage risks and implement the corporate due diligence obligations better. For instance, such an engagement facilitates information gathering about stakeholders’ interests, adverse impacts and even risks and opportunities for the company, and could lead to avoiding litigation or liability costs, reputational damage or even bring to the surface new opportunities for sustainable (long-term, green and fair) profit-making. It also contributes to building lasting business relationships and makes it easier for the company to implement its strategy successfully. Engagement with stakeholders can also give feedback on the effectiveness of the company’s due diligence measures.

# Description of the policy options

### The options contain different variations of the general and specific duties, including variations for the scope of some of the duties:

|  |  |
| --- | --- |
| **Duty** | **Scope** |
| General duty: clarifying directors’ duty to act in the interest of the company | All limited liability companies |
| Duty to manage sustainability risks  Duty to engage with stakeholders | All companies falling under the CSRD (i.e. large companies (above 250 employees and EUR 40 million turnover), listed + medium companies above 50 employees in high risk sectors and listed SMEs phased in (same scope as option 4 under due diligence) |
| Duty to set up and oversee the implementation of corporate due diligence processes and measures | Companies falling under the scope of the middle ground due diligence option |
| Sustainability strategy with science based targets | all companies under the scope of middle ground due diligence option OR a more limited scope of companies (above 1000 employees), or  All companies falling under the CSRD (i.e. large companies (above 250 employees and EUR 40 million turnover), listed + medium high risk companies and listed SMEs phased in |

### Option 1

In this option, **the general duty** to take into account the interests of stakeholders when acting in the interest of the company **would apply to all limited liability companies** as such a duty is generally regulated in civil codes or company codes, applicable to all (limited liability) companies.

Apart from the general duty this option would include only one specific duty, i.e. an **obligation to manage risks to the company related to stakeholders (sustainability risks).** As the NFRD already includes reporting obligations as regards risks, any less ambitious option on risk management is unlikely to bring sufficient impact. To ensure coherence with the scope of the CSRD proposal, the risk management duty would apply to large (according to the definition of the Accounting Directive) and listed companies and, similarly to the approach chosen for due diligence, high-impact medium-sized companies and listed SMEs would be phased in. The approach to the selection of high-impact companies is the same as for due diligence.

**All other specific duties would only be included in a Commission recommendation** for large and high impact medium-sized companies.

This option is therefore a combination of a strictly minimum regulatory measure with non-regulatory measures.

|  |  |  |  |
| --- | --- | --- | --- |
| **Option 1:** | | | |
| **Company category**  **(EU LLCs)** | **Definition** | **No. of LLCs under risk management duty** | **No. of LLCs under corporate strategy setting duty including science-based target** |
| **Large** (as under CSRD**)** | as defined in Accounting Directive, in all sectors | 65 040 | 0 |
| **Listed non-micro SMEs** (as under CSRD**)** | as defined in Accounting Directive, in all sectors (out of which listed medium-sized in high-impact sectors: 230) | 1 410 | 0 |
| **Non-listed medium-sized (simpl. def.) in high-impact sectors** | 50 < employees ≤ 250 AND 8 m < turnover ≤ 40 m (EUR) in high-impact sectors (100%), excluding listed medium-sized in high-impact sectors) | 28 510 | 0 |
| **Total number of companies incurring additional cost:** | | 94 960 | 0 |

### Option 2

As regards the general duty and risk management the approach is the same as for option 1. As regards impact management, it would include a **duty for directors to set up and oversee the implementation of due diligence measures, integrate sustainability into the corporate strategy including science-based targets applicable for very large companies, defined as above the midcap size in option 3a and 3b for corporate due diligence (**i.e. (a) above 500 employees or a turnover of EUR 350 million or (b) above 500 employees and EUR 150 million turnover). In addition, these duties would also apply to other large companies (midcaps) and medium-sized companies in high impact sectors after a phase-in period.

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Option 2:** | | | | |
| **Company category**  **(EU LLCs)** | **Definition** | **No. of LLCs under risk management duty** | **No. of LLCs under corporate strategy setting duty including science-based target** | |
| **Large** (as under CSRD**)** | as defined in Accounting Directive, in all sectors | 65 040 |  | |
| **Listed non-micro SMEs** (as under CSRD**)** | as defined in Accounting Directive, in all sectors (out of which listed medium-sized in high-impact sectors: 230) | 1 410 |  | |
| **Non-listed medium-sized (simpl. def.) in high-impact sectors** | 50 < employees ≤ 250 AND 8 m < turnover ≤ 40 m (EUR) in high-impact sectors, excluding listed medium-sized in high-impact sectors) | 28 510 |  | |
| **Medium-sized (simpl. def.) in high-impact sectors** | 70% (as in relevant due diligence scope option) |  | 19 880 | |
| **a) Very large (def. 2)** | employees ≥ 500 OR turnover ≥ EUR 350 million in all sectors |  | 23 290 |  |
| **a) Midcaps in high-impact sectors** | 50 < employees ≤ 500 AND 8 m < turnover < 350 m (EUR) in high-impact sectors, excluding medium-sized in high-impact sectors (70%) |  | 12 590 |  |
| **b) Very large (def. 3)** | employees ≥ 500 AND turnover ≥ EUR 150 million in all sectors |  |  | 9 360 |
| **b) Midcaps in high-impact sectors** | employees > 50 OR turnover > EUR 8 million in high-impact sectors, excluding medium-sized in high-impact sectors and very large LLCs in high-impact sectors (70%) |  |  | 14 530 |
| **Total number of companies covered:** | | 94 960 | 55,990 | 44,000 |

### Option 3

The general duty would be the same as in option 1. **Specific duties would be aligned with the scope of the CSRD** and would be legally binding for all large (according to the CSRD definition), listed **and** –phased in – for **medium-sized high-impact companies** and listed SMEs, **except for the duty to set up and implement due diligence processes** and measures, which would apply to the same companies as those falling under the scope of the due diligence obligation (see above). **The duty to integrate sustainability into the corporate strategy including the science-based target setting duty applies only to large companies with more than 1000 employees.**

|  |  |  |  |
| --- | --- | --- | --- |
| **Option 3:** | | | |
| **Company category**  **(EU LLCs)** | **Definition** | **No. of LLCs under risk management duty** | **No. of LLCs under corporate strategy setting duty including science-based target** |
| **Large** (as under CSRD**)** | as defined in Accounting Directive, in all sectors | 65 040 |  |
| **Listed non-micro SMEs** (as under CSRD**)** | as defined in Accounting Directive, in all sectors (out of which listed medium-sized in high-impact sectors: 230) | 1 410 |  |
| **Non-listed medium-sized (simpl. def.) in high-impact sectors** | 50 < employees ≤ 250 AND 8 m < turnover ≤ 40 m (EUR) in high-impact sectors, excluding listed medium-sized in high-impact sectors) | 28 510 |  |
| **a) Very large (var. 2)** | employees ≥ 1000 employees |  | 8 910 |
| **Total number of companies covered:** | | 94 960 | 8 910 |

### Option 4

The general duty would be the same as in option 1. **All specific duties would be aligned with the scope of the CSRD** and would be legally binding for all large (according to the CSRD definition), listed **and** –phased in – **for medium-sized high impact companies** and listed SMEs. In this scenario, the directors’ duties are aligned with the scope of Option 4 for due diligence.

|  |  |  |  |
| --- | --- | --- | --- |
| **Option 4:** | | | |
| **Company category**  **(EU LLCs)** | **Definition** | **No. of LLCs under risk management duty** | **No. of LLCs under corporate strategy setting duty including science-based target** |
| **Large** (as under CSRD**)** | as defined in Accounting Directive, in all sectors | 65 040 | 65 040 |
| **Listed non-micro SMEs** (as under CSRD**)** | as defined in Accounting Directive, in all sectors (out of which listed medium-sized in high-impact sectors: 230) | 1 410 | 1 410 |
| **Non-listed medium-sized (simpl. def.) in high-impact sectors** | 50 < employees ≤ 250 AND 8 m < turnover ≤ 40 m (EUR) in high-impact sectors, excluding listed medium-sized in high-impact sectors) (100% / 70%) | 28 510 | 19,880 |
| **Total number of companies covered:** | | 94 960 | 86,330 |

1. Implications of the COVID-19 pandemic

# Summary

The COVID-19 crisis underscored the importance of a long-term oriented, sustainable and resilient economy. It revealed weaknesses related to short-termism, lack of resilience, unregulated global supply chains and unsustainable business models. It led to increased stakeholder attention to the impacts of companies, especially regarding workers and supply chains. It has therefore further accelerated the demand for more resilient business models and robust and sustainable supply chains. At the same time, the economic crisis generated by the pandemic makes it important to avoid the imposition of unnecessary administrative costs on business.

The Communication “[Europe's moment: Repair and Prepare for the Next Generation](https://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1590732521013&uri=COM:2020:456:FIN)” (Recovery Plan) confirmed the Commission’s intention to put forward an initiative on sustainable corporate governance with the objective to “ensure environmental and social interests are fully embedded into business strategies”. Relevant objectives are strengthening corporate resilience, improving predictability and management of risks, dependencies and disruptions including in the supply chains, with the ultimate aim for the EU economy to build back stronger.

# Impact of Covid-19 on the problem definition

A study conducted on corporate resilience during the first wave of the COVID crisis[[363]](#footnote-364) analyses which companies weathered the first shock of the crisis better. The research suggests that firms that invested more in corporate social responsibility activities prior to the pandemic enjoyed much better stock price performance in response to the pandemic. A study published by the European Capital Markets Institute finds that “companies integrating an ESG approach recognised by investors and ESG funds have been more resilient in the crisis”, and goes on to conclude that “investors’ taste for ESG has not lessened during this crisis – quite the opposite, in fact.”[[364]](#footnote-365)

Furthermore, the results of a recent EC survey[[365]](#footnote-366) illustrated the impact the COVID-19 crisis had on consumption patterns in terms of consumers making ‘greener' choices. 56% of consumers said environmental concerns influenced their purchasing decisions and 67% said that they bought products that were better for the environment, even if such products were more expensive. These results are consistent with the view that investments in social and environmental performance build trust with stakeholders, so that workers, suppliers, customers, and other stakeholders are more willing to make adjustments to support the business in response to adverse shocks. The estimated impact is robust and economically large.

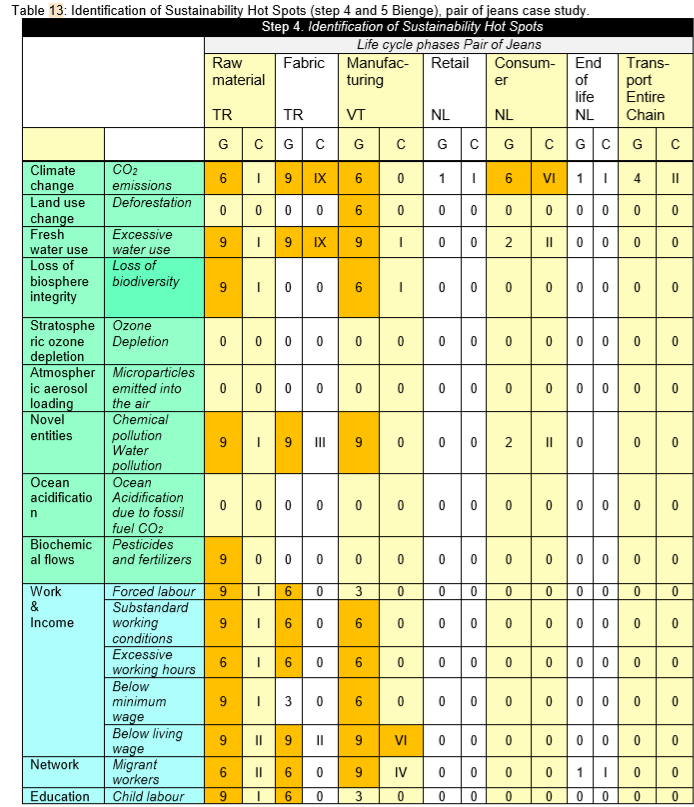
More generally, the pandemic may contribute to a greater awareness of the complex interactions between environmental degradation, social problems and the health of the economy.[[366]](#footnote-367) One informed analyst has stated that “the health crisis now ravaging all continents has put the spotlight on vulnerabilities and our dependence on the natural environment. It drives home the message that markets do not operate in isolation, but instead are embedded in societies and the natural environment. This realization will fundamentally change our long-term risk perspective and the way we prepare for the looming climate crisis.”[[367]](#footnote-368)

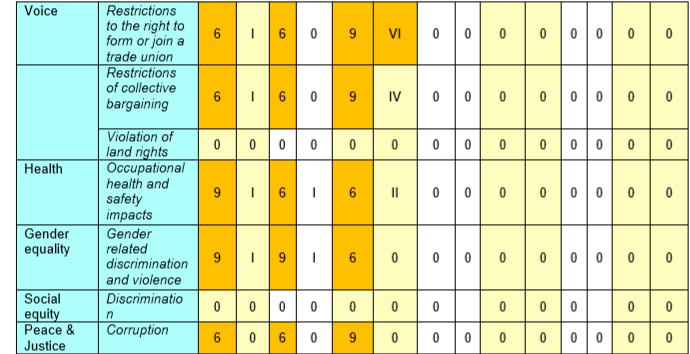
# Impact of Covid-19 on the policy options

The economic crisis generated by the pandemic makes it even more important to avoid the imposition of unnecessary administrative costs on business, especially SMEs. This has also been highlighted by respondents to the open public consultation on this initiative who stress that “the potential benefits must be seriously balanced against the potential harm in a highly vulnerable situation”. First of all, it has to be noted that companies subject to any new requirements under this initiative would not have to dedicate resources to meeting such requirements until 2024 at the earliest. One-off costs could have a negative short-term impact on competitiveness of EU companies which are competing with third country companies. Such impact will depend on the sector. However, as third country companies having significant turnover in the EU are meant to be covered by due diligence, this will further reduce any possible negative impacts on cost competitiveness in the short term. In the mid to longer-term, all evidence points to better performance and more resilience. Furthermore, one-off and recurrent costs could present a bigger burden for high-risk SMEs which have no experience with due diligence so far. The numerous measures mitigating the negative cost impact on SMEs have been explained in detail in the impact assessment report and are not reiterated here.

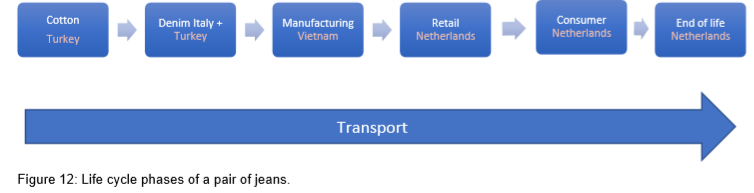
1. The garment value chain: direct and indirect suppliers and where the main impacts are

The table below is an extract from the *SMART Sustainability Hot Spot Analysis of two ready-made garments*.[[368]](#footnote-369) It identifies the sustainability hotspots in the lifecycle of a pair of jeans.[[369]](#footnote-370)





Below is an overview of the lifecycle of that pair of jeans:



1. Intervention logic



1. International Human Rights and Environmental Conventions

The following lists include multilateral international conventions specifying harmful activities from a human rights and environmental point of view:

**International environmental conventions**

|  |  |  |
| --- | --- | --- |
| **International convention** | **Concrete obligations that can be complied with by companies** | **Legal act already referencing the convention for compliance by companies, including in their value chains** |
| Paris agreement (OJ L 282, 19.10.2016, p. 4) and the [United Nations Framework Convention on](https://unfccc.int/resource/docs/convkp/conveng.pdf)  [Climate Change](https://unfccc.int/resource/docs/convkp/conveng.pdf) | Net-zero greenhouse gas emissions from companies’ activities by mid-century or before |  |
| Post 2020 Convention on Biodiversity | Tbc, new convention expected in 2022.  The most recent [draft](https://www.cbd.int/doc/c/abb5/591f/2e46096d3f0330b08ce87a45/wg2020-03-03-en.pdf) of the post 2020 Convention on Biodiversity includes 2030 action targets. This includes [target 15](https://www.cbd.int/sites/default/files/2021-08/gbf_one_pager_target_15.pdf), whereby all businesses (public and private, large, medium and small) assess and report on their dependencies and impacts on biodiversity, from local to global, and progressively reduce negative impacts, by at least half and increase positive impacts, reducing biodiversity-related risks to businesses and moving towards the full sustainability of extraction and production practices, sourcing and supply chains, and use and disposal | [Proposal for a Regulation concerning batteries and waste batteries](https://ec.europa.eu/environment/pdf/waste/batteries/Proposal_for_a_Regulation_on_batteries_and_waste_batteries.pdf), repealing Directive 2006/66/EC and amending Regulation (EU) No 2019/1020, recital 68. [[370]](#footnote-371) |
| Vienna Convention for the protection of the Ozone Layer and its Montreal Protocol on substances that deplete the Ozone Layer | Eliminate the production of nearly 100 substances that deplete the ozone layer. | [Directive 2014/24/EU](https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014L0024&from=en) of 26 February 2014 on public procurement, Annex X[[371]](#footnote-372) |
| Basel Convention on the Control of Transboundary Movements of Hazardous Wastes and their Disposal (Basel Convention) | Ensure that the generation of hazardous wastes and other wastes is reduced to a minimum  Ensure environmentally sound management of hazardous wastes  Prevent pollution due to hazardous wastes and minimize the consequences of such pollution  Transboundary movement of hazardous wastes and other wastes is reduced to the minimum | [Directive 2014/24/EU](https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014L0024&from=en) of 26 February 2014 on public procurement, Annex X371 |
| Stockholm Convention on Persistent Organic Pollutants (Stockholm POPs Convention) | Eliminate production and use of intentionally produced POPs,  Eliminate unintentionally produced POPs, manage and dispose of POPs wastes in an environmentally sound manner | [Directive 2014/24/EU](https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014L0024&from=en) of 26 February 2014 on public procurement, Annex X371  German Law on Corporate Due Diligence in Supply Chains, Annex (a previous version of the law can be found [here](https://www.bmas.de/SharedDocs/Downloads/DE/Gesetze/Regierungsentwuerfe/reg-sorgfaltspflichtengesetz.pdf?__blob=publicationFile&v=2), the Annex has not changed compared to the previous version) |
| Convention on the Prior Informed Consent Procedure for Certain Hazardous Chemicals and Pesticides in International Trade (UNEP/FAO) (The PIC Convention) Rotterdam, 10 September 1998, and its 3 regional Protocols | The Convention places obligations on companies who wish to export the chemicals covered to non-EU countries | [Directive 2014/24/EU](https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014L0024&from=en) of 26 February 2014 on public procurement, Annex X371 |
| Minamata Convention on Mercury | No more mercury mining, restriction or phase-out of manufacturing processes in which mercury is used  Control or reduction of emissions of mercury to the atmosphere and reduction of releases of mercury to land and water through measures to control emissions | German Law on Corporate Due Diligence in Supply Chains, Annex (a previous version of the law can be found [here](https://www.bmas.de/SharedDocs/Downloads/DE/Gesetze/Regierungsentwuerfe/reg-sorgfaltspflichtengesetz.pdf?__blob=publicationFile&v=2), the Annex has not changed compared to the previous version) |
| International Convention on Civil Liability for Oil Pollution Damage (CLC Convention) | It establishes strict liability in case of oil pollution damage and includes an insurance requirement. | n/a |
| *Cartagena Protocol on Biosafety (2000)*  *[under consideration]* | *It seeks to protect biological diversity from the potential risks posed by genetically modified organisms resulting from modern biotechnology*  *The Protocol applies to the transboundary movement, transit, handling and use of all living modified organisms that may have adverse effects on the conservation and sustainable use of biological diversity, taking also into account risks to human health.* | *n/a* |
| *Convention on International Trade in Endangered Species of Wild Fauna and Flora (1973)*  *[under consideration]* | *It seeks to prevent species from becoming endangered or extinct because of international trade.*  *All import, export, re-export and introduction from the sea of species covered by the convention has to be authorized through a licensing system.* | *n/a* |

**International human rights conventions**

* **The nine ILO fundamental Conventions** (plus the Protocol of 11 June 2014 to International Labour Organisation Convention No. 29 of 28 June 1930 concerning forced or compulsory labour):
* **Forced or compulsory labour** Convention No. 29 of 28 June 1930;
* Convention No. 87 of 9 July 1948 concerning **freedom of association and protection of the right to organise,** as amended by the Convention of 26 June 1961;
* Convention No. 98 of 1 July 1949 concerning the Application of the Principles of the **Right to Organise and to Bargain Collectively**, as amended by the Convention of 26 June 1961;
* Convention No. 100 of 29 June 1951 concerning **Equal Remuneration for Men and Women Workers for Work of Equal Value**;
* Convention No. 105 of 25 June 1957 concerning the **Abolition of Forced Labour**;
* Convention No. 111 of 25 June 1958 concerning **Discrimination** in Respect of Employment and Occupation;
* Convention No. 138 of 26 June 1973 concerning the **minimum age** for admission to employment;
* Convention No. 182 of 17 June 1999 concerning the **Prohibition and Immediate Action for the Elimination of the Worst Forms of Child Labour**;
* Convention No. 183 concerning **Maternity Protection**, (Revised), 1952 (Entry into force: 07 February 2002);
* The **International Covenant on Civil and Political Rights**;
* The **International Covenant on Economic, Social and Cultural Rights**;
* **Convention on the Rights of the Child**.

1. EU Supporting Measures

**Accompanying measures to SUPPORT THE implementation of the proposed EU INITIATIVE on sustainable CORPORATE GOVERNANCE AND due diligence in SUPPLY CHAINS**(ongoing actions, MFF 2014-2020)

| **Action (lead service)** | **Description / objective** | **Type of EU support** | **Target groups** | **Sector** | **Region** | **Implemen­ting partners** | **Budget (instrument)** | **Timeline** | **Supported legislation** |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **information and Guidance on Due Diligence process and Legal Requirements** | | | | | | | | | |
| **Due Diligence Ready! Portal**  (DG GROW) | This online portal contains in 7 languages information, tools and training materials to guide especially small and medium sized EU company in conducting due diligence on their minerals and metals supply chain in compliance with regulatory requirements, including Responsible Mining Regulation.  The objectives of the portal are to help companies (i) learn about the benefits companies can gain from performing due diligence on their supply chains; (ii) understand, assess and mitigate risks and impacts in their supply chains; and (iii) understand and implement the OECD due diligence guidance for responsible supply chains of minerals from conflict-affected and high-risk areas. | Online portal | EU SMEs | Minerals | global | Contractor | - |  | RMR, SGCI |
| **Guidance on Due Diligence for EU businesses to address the risk of forced labour in their operations and supply chains**  (DG TRADE / EEAS) | In light of the growing level of public attention to the issue of forced labour and its potential implications for the activities of EU companies, the Commission and EEAS have prepared guidance to assist EU companies to carry out effective due diligence in order to identify, mitigate and prevent the risk of forced labour in their operations and supply chains. The Guidance, which was announced in the 2020 Trade Policy Review Communication, exclusively relies on existing international standards on due diligence, and does not create new obligations for companies. | Guidance document | EU companies | Horizontal | global | - | - | 2021 - | SCGI |
| **Toolkit on Business and Human Rights**  (DG INTPA, EEAS) | Practical guidance to colleagues in EU Delegations on how to implement the policy framework on Business and Human Rights through existing development cooperation modalities. Toolkit is designed for internal use. It could also be made available to EU Member States agencies. | Guidance document | EU Delegations and MS agencies | Horizontal | Global | Danish Institute for Human Rights | - | Published in 2021 | SCGI |
| **OECD E-learning Academy on Responsible Business Conduct**  (EEAS) | The OECD E-learning Academy on RBC provides companies and interested stakeholders with a unique opportunity to advance their knowledge on responsible business conduct (RBC) and OECD risk-based due diligence. | Grant | Lead firms, suppliers, stakeholders | Horizontal | Global | OECD RBC Centre | Instrument contributing to Stability and Peace (IcSP) | 2020-2022 | SCGI |
| **Better Work Academy** | Aimed at brands and other actors committed to driving change and transforming behaviour in the apparel industry, the Better Work Academy provides training and advisory services building capacity to implement the better Work Programme’s tried-and-tested methodologies across the supply chain. | Grant | Companies and actors along garment supply chain | Textiles | Global | ILO | Indirectly supported through EU co-financing of BW Prg. |  | SCGI, Textiles Strategy |
| **ITC SME Academy** | Offers courses on standards and sustainability:   * The Role of Standards in Sustainable SCs * Competitiveness Through Enterprise Sustainability * Becoming a Climate Resilient SME * Meeting Standards in the Agrifood Sector * Introduction to Standards and Sustainability | Online courses | Trade Advisors  Policy Makers  Companies | Horizontal | Global | ITC | Different donors (including EU) | Ongoing | SCGI |
| **practical tools for Supply Chain Management, Risk Assessment and Reporting** | | | | | | | | | |
| **Enhancing decent work, transparency and traceability for sustainable value chains in the garment and footwear industry**  (DG INTPA) | Component 1 aims at developing a global standard for traceability in the garment sector through setting up a multi-stakeholder policy platform, developing policy recommendations traceability standards and implementation guidelines.  Component 2 consists of the creation of a social and sustainability audits database by operating an open source database with voluntarily shared results of the social and sustainability audits of companies, and ensuring the compatibility of audit formats through Common Assessment Framework developed by over 200 textile operators of the Social & Labor Convergence Program. | TA grant | Global brands and local companies in garment and footwear supply chain | Textiles | Global | UNECE- UN/CEFACT (comp. 1);  ITC  (comp. 2) | EUR 4.2 Mio. (GPGC) | 2019-2022 | SCGI, Textiles Strategy |
| **ITC Trade and Market Information (TMI) tools**  (DG INTPA) | ITC’s TMI tools include:   * Sustainability Map: “One stop shop” acting as a global public repository of neutral and trusted information about businesses’ sustainability credentials * Trade Map: presents international trade statistics with useful indicators on current trade performance. * Market Access Map: web application to analyse market access conditions applied by more than 200 countries. * Export Potential Map: innovative tool to identify products, markets and suppliers with (untapped) export potential. * RoO Facilitator: Online portal designed to help MSMEs understand applicable rules of origin to their product. * Market Price Information: Tool to track recent market price information from multiple sources and geographical areas. * Procurement Map: Contains more than 250,000 active public tenders and contract awards from 180 countries updated daily. * Investment Map: tool combining statistics on FDI, int. trade, market access conditions. | Grant | SMEs (exporters, importers), brands, private standard schemes, TISIs, | Horizontal | Global | ITC | EUR 5 Mio. (CPGC) | 2019 - 2022 | SCGI |
| **Hidden Homeworkers – Improving Transparency and Traceability to Improve Working Conditions of Homeworkers in Apparel and Footwear Chains**  (DG INTPA) | Grant contract awarded as part of the Call for Proposal “Increasing Knowledge, Awareness, Transparency and Traceability for Responsible VCs in the Cotton and Garment Sectors”  The project aims to work collaboratively with brands and multi-stakeholder initiatives to map supply chains down to the homeworker level. It helps brands introduce simple systems that document homeworkers’ contribution and wages, and develop action plans that drive transparency, best practices and improve working conditions. | Action grant (CfP) | Home-workers | Textiles | India, Nepal, Pakistan | TRAIDCRAFT Exchange | EUR 1 Mio. (76% of project costs) | April 2019 - March 2023 | SCGI, Textiles Strategy |
| **Towards Mutual Buyer-Supplier** **Collaboration: Supplier Capacity & Better Buying Platform**  (DG INTPA) | Grant contract awarded as part of the Call for Proposal “Increasing Knowledge, Awareness, Transparency and Traceability for Responsible VCs in the Cotton and Garment Sectors”  The project aims to develop an online tool (Supplier Capacity Platform) that incentivizes supply chain transparency and visibility and improves buyer-supplier dialog and workflows. By targeting 3-5 European clothing brands and retailers and 50 suppliers in Bangladesh, the action seeks to improve transparency and traceability through the value chain, enhance business due diligence efforts and promote responsible production; and strengthen multi-stakeholder collaboration to promote responsible sourcing and production. | Action grant (CfP) | Local garment factories | Textiles | Bangladesh | Social Accountability International | EUR 0,625 Mio. (50% of project costs) | March 2019 – Feb. 2022 | SCGI, Textiles Strategy |
| **EU REDD+ Facility**  **Programme to combat deforestation in the context of climate change**  (DG INTPA) | The Facility was established in 2010 to support developing countries in improving land-use governance as part of their efforts to slow, halt and reverse deforestation. It also supports the overall EU effort to reduce its contribution to deforestation in developing countries. The Facility focuses on countries that are engaged in REDD+, an international mechanism that incentivises developing countries to reduce greenhouse gas emissions from their forest and land-use sectors.  The Facility cooperates with the TRASE (Transparency of Sustainable Economies) initiative, which makes use of a mass of untapped production, trade and customs data for a set of agricultural commodities. | TA | Partner country gov.; companies along agricultural supply chains (esp. cocoa, palm oil) | Agriculture, Forestry | Côte d’Ivoire, Cameroon, Congo, DRC, Colombia, Ecuador, Indonesia, Vietnam, and Laos | European Forest Institute (EFI) | EUR 6 Mio. | 2018 - 2023 | SCGI, EU Sustainable Cocoa Initiative; Deforestation Regulation |
| **World Benchmarking Alliance (WBA)**  (DG INTPA) | WBA is a multi-stakeholder platform having as its core mission the promotion of dialogue and action around the role of business in achieving the SDGs. Its main result will be the creation of a widely accepted methodology and benchmarking framework that can be used for comparing companies’ performance and impact towards the achievement of the SDGs. By 2023, the WBA will assess the progress of 2,000 companies across seven major areas of transformation required to achieve the SDGs: Social, Digital, Food and Agriculture, Urban, Decarbonisation and Energy, Circular, Financial. | Co-financing grant | EU/internat. policy- makers and private sector | Horizontal | Global | Dutch Ministry of Foreign Affairs | EUR 1 Mio. (GPGC) | 2020 - 2022 | SCGI |
| **Align project - Aligning accounting approaches for nature**  (DG ENV) | The project assists the EU’s efforts to support businesses and other stakeholders in developing standardised natural capital accounting practices, including a standardised approach to biodiversity measurement. The project includes the drafting of recommendations for a standard on biodiversity measurement and valuation, and related guidance applicable to site-based and supply chain companies, as well as the finance sector. | Services contract | EU companies and their supply chains | Horizontal - biodiversity | Global | WCMC Europe, the Capitals Coalition, Arcadis, ICF and UNEP-WCMC |  | 2021 - 2024 | SCGI |
| **Global Policy Dialogue, International COORDINATION and Research** | | | | | | | | | |
| **Global action to end Child Labour**  (DG INTPA) | The proposed Action will consolidate and structure the EU commitments to eradicate child labour. It will support activities to address knowledge gaps, build global evidence and reinforce advocacy in international fora and business networks through root causes analysis, data sharing and technical expertise. Another related objective is to contribute to global initiatives and partnerships such as the Alliance 8.7. | Grants | Key actors at all levels engaged in eradicating child labour | Horizontal | Global | Specialised IOs, CSOs, ILO | EUR 10 Mio. (Global Challenges-Prosperity) | 2022-? | SCGI |
| **SWITCH to Green** **Facility**  (DG INTPA) | Support efforts to contribute to the green economy transition across the broader EU international cooperation portfolio, notably through quality support to new actions in relevant sectors. It generally supports the SWITCH initiatives. | TA | Government, CSOs, private sector operators, international bodies | Horizontal | Global | Adelphi Consult GmbH | EUR 7.7 Mio. (includes funds for Water Facility since 2020) | 2015 - 2022 | CEAP; SCGI |
| **OECD Responsible Minerals Programme**  (EEAS) | Support of the OECD’s work on responsible minerals incl. research, organisation of annual Forum on Responsible Mineral Supply Chains, minerals alignment assessment etc. | Grants | EU, policy-makers, actors along minerals supply chain | Minerals | Global | OECD RBC Centre | EUR 3 Mio. (75% of total programme cost) (IcSP) | 2020 - 2023 | RMR, SCGI |
| **OECD Garment Supply Chain work**  (DG TRADE) | Partial funding of OECD’s work on RBC in the garment sector, incl. work to convene stake-holders, capacity building in the garment & footwear sector, incl. annual Forum on Due Diligence in the garment & footwear sector, roundtable for policy makers and manufacturers network; garment sector alignment assessments, country engagement and research. | Grants | EU, policy-makers, actors along garment & footwear supply chain | Textiles | Global | OECD RBC Centre | EUR 0,8 Mio. | 2020 - 2022 | SCGI, Textiles Strategy |
| **Industry collaboration AND stakeholder engagement** | | | | | | | | | |
| **Cocoa Talks**  (DG INTPA, DG TRADE) | Under the Sustainable Cocoa Initiative, DG TRADE and DG INTPA are jointly organising thematic roundtables that look into various aspects of the sustainability of the cocoa supply chain, including living income for farmers, sustainability standards, traceability in respect to child labour and deforestation, regulation with the focus on due diligence, sustainable production of cocoa and its support through development cooperation. These multi-stakeholder discussions serve guide the way forward in the EU’s collaboration with cocoa producing countries, the private sector and CSOs on improving sustainability of the cocoa supply chain. | Multi-stake-holder dialogue | Cocoa supply chain actors (industry, traders, farmers, NGOs, Member States and partner countries) | Agriculture – cocoa | Ghana, Cote d’Ivoire, Cameroon |  |  | Sept. 2020 - – Nov. 2021 | SCGI, Sustainable Cocoa Initiative, Deforestation Regulation |
| **European Partnership for Responsible Minerals (EPRM)**  (DG INTPA) | The EPRM is a multi-stakeholder partnership between governments, private sector supply chain actors and CSOs with the objective to increase the proportion of responsibly produced minerals from conflict-affected and high-risk areas (CAHRAs) and to support socially responsible extraction of minerals that contributes to local development. The partnership accompanies implementation of the EU Conflict Minerals Regulation in that it enable more mines to comply with the standards required under the OECD Due Diligence Guidance. | Co-financing grant | EU and local companies along minerals supply chain | Minerals | Global (CAHRAs) | Netherland Enterprise Agency (RVO) | EUR 7 Mio. | 2018 - 2024 | RMR; SCGI; Action Plan on Critical Raw Materials |
| **Producer/Supplier capacity building and EMpowerment** | | | | | | | | | |
| **SWITCH to Circular Economy Value Chains**  (DG INTPA) | The initiative promotes the adoption of circular economy practices in selected value chains, green and decent job creation, and the green economy transition. It targets private sector operators, notably Micro, Small and Medium Enterprises (MSMEs) and local financial institutions. Expected Outcome 1: Improved business environment for the uptake of circular economy approaches in targeted countries; Expected Outcome 2: Improved circularity amongst private operators of selected value chains. | TA, Grants | MSMEs, Local FIs | Horizontal | Global | UNIDO | EUR 19mln | 2020-2025 | CEAP; SCGI |
| **SWITCH Africa Phases** **I and II**  (DG INTPA) | The overall objective of the programme is to contribute to poverty reduction in Africa in the context of sustainable development through support to private sector-led inclusive green growth which fosters transformation towards a green economy. The programme supports:  (i) the establishment of policies, incentive structures, and instruments for green business development; and  (ii) private sector initiatives promoting SCP practices. Phase II is in line with Phase I but has three complementary components (policy support, green business development through grants to private sector initiatives, networking facility). | TA, Grants | MSMEs | Horizontal | Burkina Faso, Ethiopia, Ghana, Kenya, Mauritius, South Africa, Uganda | UNEP | EUR 23.5mln | 2014-2022 | CEAP, SCGI |
| **SWITCH Asia**  (DG INTPA) | The overall objective of the SWITCH Asia programme is to promote sustainable growth, to contribute to poverty reduction and to foster climate change mitigation while decoupling economic growth from environmental degradation. Incorporates a grant scheme for SCP, an SCP Facility and a regional policy advocacy component. | TA, Grants | MSMEs, Government (different levels) | Horizontal | Asia |  | EUR 32.8 Mio  (new EUR 20 Mio. planned under AAP21) | 2019 - 2026 | CEAP; SCGI |
| **AL-INVEST Verde (EU- Latin America Alliance for Sustainable Growth and Jobs)**  (DG INTPA) | The programme supports the transition towards a low-carbon, resource-efficient and a more circular economy in Latin America, while helping countries adopt sustainable consumption patterns.  *Component 1*: Grant scheme (CfP) for private sector intermediaries/SMEs innovative actions aiming at more sustainable economic practices, built through alliances between LAC and EU companies.  *Component 2*: Policy advocacy for effective implementation of core environmental and labour standards in line with commitments enshrined in the Trade and Sustainable Development chapters of trade agreements  *Component 3*: Support to more efficient and user-friendly Intellectual Property protection and enforcement systems. | Action grants (through CfPs) and TA | EU and LA SMEs; business intermediaries, research institutes, public authorities, local public bodies | Horizontal | Latin America | *Component 1:* Consortium of EU-LAC business intermediaries  *Component 2:* EU MSs agencies  *Component 3:* EUIPO | EUR 33 Mio.  (Component 1: EUR 25 Mio.; Component 2: EUR 6 Mio; Component 3: EUR 2 Mio  [DCI (2014-2020 RIP)] | 2020-2026 | SCGI; Deforestation Regulation |
| **EU-ACP Development Minerals Programme**  (DG INTPA) | The programme provides capacity-building support to the artisanal and small-scale private sector, associations / chambers, public institutions and social stakeholders that operate in the low-value minerals and material sector. | TA grant | Artisanal, small-scale miners | Minerals | ACP countries | UNDP | EUR 12 Mio. (phase 1)  EUR 10 Mio. (phase 2) | 2014 -2019 (phase 1)  2020 - 2025 (phase 2) | RMR; Action Plan on Critical Raw Materials |
| **Better Work programme**  (DG INTPA) | The programme brings together all levels of the garment industry to improve working conditions and respect of labour rights for workers, and boost the competitiveness of apparel businesses.  Currently, the programme is active in 1.700 factories employing more than 2,4 million workers in nine countries. As a result of their participation with Better Work, factories have steadily improved compliance with ILO core labour standards and national legislation covering compensation, contracts, occupational safety and health and working time.  Better Work also collaborates with govern­ments to improve labour laws, and is advising unions on workers’ rights and participation. | TA grant (ind. mgnt) | Local garment industry, global bands, governments, unions | Textiles | Bangladesh, Cambodia, Egypt, Ethiopia, Haiti, Indonesia, Jordan, Nicaragua, Vietnam  *As of 2021*: Sri Lanka, Pakistan, Madagascar | ILO, IFC | EUR 14,8 Mio. | 2019 - 2022 | SCGI, Textiles Strategy |
| **Vision Zero Fund**  (DG INTPA,  DG EMPL) | VZF is an initiative of the G7, endorsed by the G20. Donors include the European Commission, France, Germany, and the US.  The multi-donor Vision Zero Fund (VZF) works to reduce the number of work-related fatalities and accidents and occupational diseases in selected developing countries, in sectors that link to GSCs (garment, agriculture - coffee, ginger cotton, and construction), as well as adequately compensating victims and their families in case of such accidents. The VZF brings together governments, employers’ and workers’ organizations, companies, and other stakeholders to jointly advance towards the vision of achieving zero severe and fatal work-related accidents, injuries and diseases in global supply chains. | TA grant | governments, social partners, companies | Textiles, agriculture | Ethiopia, Lao PDR, Madagascar, Myanmar, Colombia, Honduras Mexico, Vietnam | ILO (GIZ) | EUR 3 Mio. (ILO); EUR 0,5 Mio. (GIZ ext. monitoring)  EUR 2,3 Mio. by DG EMPL | 2017-2021  (EMPL to continue funding till 2022 and potentially beyond) | SCGI, Textiles Strategy |
| **Ethical Fashion initiative (EFI)**  (DG INTPA) | The EFI promotes the creation of decent jobs and sustainable development of micro-enterprises in the handicraft sector through responsible and ethical management of specific value chains linked to the fashion industry, lifestyle and interior design sectors in Burkina Faso and Mali. The overall theory of change is for the project to support the emergence of sustainable communities of artisans organized within recognized social businesses and empower them to access international textile value chains while supporting the development of end products made in Africa for export. | TA grant | Local micro-enterprises in handicraft sector | Textiles | Burkina Faso, Mali | ITC | EUR 10 Mio. | 2017-2021 | SCGI |
| **Market Access Upgrade (MARKUP) Programme**  (DG INTPA) | Supports efforts in the development of value chains and exports in agro-industrial crops (coffee, tea and cacao) and horticulture, supporting participation in regional and global value chains. Interventions cover quality assurance and certification, value addition, trade facilitation, enhancement of SME export competitiveness and business development services. | TA grant | Companies along coffee, tea and cocoa supply chain | Agriculture | East African Community (Burundi, Rwanda, Tanzania, Kenya, South Sudan, Uganda) | GIZ, ITC, UNIDO, Solidaridad | EUR 35 Mio. | 2018-2022 | SCGI |
| **Support to Rural Entrepreneurship, Investment and Trade in Papua New Guinea**  (DG INTPA) | The action supports the sustainable and inclusive economic development of rural areas through a combination of two integrated outcomes:  (1) Increasing the economic returns and opportunities from cocoa, vanilla and fishery through improved value chain development.  (2) Strengthening and improving the efficiency of value chain enablers including the business environment and supporting sustainable, climate proof transport and energy infrastructure development. | TA grant | Local actors along cocoa, vanilla and fishery supply chains | Agriculture | Papua New Guinea | FAO, UNDP, ILO, ITU, UNCDF | EUR 85 Mio ? | 2019-2024 | SCGI |
| **A4A Eswatini: Promoting growth through competitive alliances**  (DG INTPA) | The overall objective of the action is to improve livelihoods of smallholder farmers and workers in Eswatini by creating better jobs and growth. The implementation applies the ITC’s “Alliance for Action“ (A4A) approach that involves building up alliances that bind value chain actors in collectively upgrading MSMEs, value-chains and support services in an environmentally and socially responsible manner, including value addition, public private dialogue and strong anchoring in markets. | TA | MSMEs, Smallholder farmers  Arts and crafts producers  Trade and Investment Support institutions (TISI) | Agriculture, Arts, Crafts | Eswatini | ITC | EUR 5 Mio | 2020-2024 | SCGI |
| **ACP: Strengthening Productive Capabilities and Value Chain Alliances**  (DG INTPA) | With major focus on the development of agriculture and agri-business value chains, the Programme is designed to achieve two key outcomes: (1) adopting and implementing business-friendly, inclusive and responsible national policies and legal frameworks, and (2) strengthening productive, processing, promoting and marketing capabilities and value chains.  The aim is to address the main local issues around the social, environment, economic aspects while improving the transparency and the traceability of their supply chains. | TA | Smallholder farmers, MSMEs; Support Institutions, Policymakers | Agriculture Coffee, Cotton, Cocoa, Kasava,  Coconuts | ACP countries | ITC | EUR 17.23 (11th EDF)  The total budget is 34.7 million EUR and is distributed across three Agencies: ITC World Bank Group and UNIDO | 2018 - 2023 | SCGI |
| **Alliances for Coconut Industry Development in the Caribbean  (I and II)**  (DG INTPA) | Facilitates alliances among actors at every step of the coconut value chain. Revival of the industry will increase food availability and incomes of small-scale farmers through improved competitiveness of the coconut sector.  Phase I of the Development of the Coconut Industry for the Caribbean project has catalyzed investment and ramped up productive and commercial capacity amongst beneficiaries. It has improved value capture and productive and governance capacities.  Phase II aims to replicate the successful partnerships model across the Caribbean region and scale up impact through the Alliances for Action model by adopting an inclusive and participatory approach | TA | Smallholder farmers, MSMEs; Support Institutions, Policymakers | Agriculture Coconuts | Antigua and Barbuda, Barbados, Belize, Dominica, Dominican Republic, Grenada (Phase II), Guyana, Jamaica, St. Lucia, St. Vincent and Grenadines, Suriname, Trinidad and Tobago | ITC; ACP- Cariforum | USD 3.9 Mio (Phase 1)  USD 6.7 Mio (Phase II) | 2015 - 2018  2019 - 2023 | SCGI |
| **Strengthening the Agriculture and Agri-food Value Chain and Improving trade policy in Iraq (SAAVI)**  (DG INTPA) | SAAVI contributes to inclusive economic growth and job creation, particularly for youth, by improving Iraq’s agriculture competitiveness and supporting trade development. The project forms part of the overall EU special measure for supporting employment creation and improving economic governance in Iraq. | TA | Agri-MSMEs;  Farmers groups and producers organization; Trade support institutions; industry associations | Agriculture Horticulture Poultry | Iraq | ITC | USD 22 Mio. | 2021 - 2025 | SCGI |
| **ARISE+ Laos**  (DG INTPA) | ARISE+ promotes inclusive economic growth, climate change resilience, mitigating vulnerability and job creation in the Lao People's Democratic Republic.  The project gears towards improving the country's overall business environment and increasing its participation in global value chains in two sectors: wood processing and coffee. Capacity building on organic coffee and certification. | TA | MSMEs, TISIs | Agriculture Coffee, Wood | Laos | ITC | USD 5.45 Mio | 2018 - 2022 | SCGI |
| **Bhutan (Honey, Chilli and Mushrooms)**  (DG INTPA) | The action focuses on two value chains, horticulture and textile handicrafts, as well as cross-cutting trade policy issues. It aims at enhancing capacity in formulation and implementation of trade and investment policy and regulations; promote increased export of high value horticulture products (incl. organic), high-value handicraft textile products, ginger/turmeric and mushrooms. | TA | TISIs, MSMEs  (producers and exporters) | Garment  Textile  Horticulture | Bhutan | ITC | EUR 4.9 Mio. | 2018 - 2022 | SCGI |
| **Growth for rural advancement and sustainable progress, Pakistan (GRASP)**  (DG INTPA) | GRASP is designed to reduce poverty in Pakistan by strengthening small-scale agri-businesses in the Balochistan and Sindh provinces. It helps small and medium-sized enterprises in horticulture and livestock become more competitive by making improvements at all levels of the value chain, incl. promotion of climate-smart agriculture, improving dissemination of market information through digital tool and improving access to financing. There will be a special focus on improving sustainability by enabling firms to acquire the appropriate technology. | TA | TISIs, MSMEs  (producers and exporters) | Horticulture Livestock | Pakistan | ITC | USD 53.5 Mio | 2019 - 2024 | SCGI |
| **Regulatory environment and support ecosystem in Partner Countries** | | | | | | | | | |
| **BHR in Asia:  Enabling Sustainable Economic Growth through the Protect, Respect and Remedy Framework**  (FPI) | Support the implementation of the UNGPs in close partnership with Asian governments, business, and civil society, through dialogue, training, research, small grant provision and awareness raising activities. | TA grant | Governments, local businesses, CSOs | Horizontal | India, Indonesia, Malaysia, Myanmar, Sri Lanka, Thailand | UNDP | EUR 5,5 Mio.  (Partnership Instrument, AAP 2019) | 01/01/2020-31/12/2023 | SCGI |
| **RBC in Asia** | The programme aims to help companies and governments improve respect for human and labour rights and environmental standards across global supply chains and take action to create an enabling environment for responsible business conduct.  The programme is carried out in partnership with Japan, an OECD member and the only country under the Programme that has adhered to the OECD MNE Guidelines and has set up a [National Contact Point for RBC](http://mneguidelines.oecd.org/ncps/). | Grant (indirect mgn’t) | Partner country governments, companies | Horizontal | China, Myanmar, Philippines, Thailand, Vietnam and Japan | OECD, ILO | EUR 9 Mio,  of which EUR 4,95 Mio. for OECD; and EUR 4,05 Mio. for ILO.  (Partnership Instrument, AAP 2016) | 15/12/2017- 14/06/2021 | SCGI |
| **RBC in Latin America and Caribbean**  (FPI) | Reinforcing cooperation between the EU and LAC governments and businesses on RBC. | TA grant | Partner country governments, companies | Horizontal | Argentina, Brazil, Chile, Colombia, Costa Rica, Ecuador, Mexico, Panama, Peru | OECD, ILO, UNOHCHR | EUR 9,5 Mio.  of which EUR 3,264,380 for OECD; EUR 6,235,620 for ILO/OHCHR.  (Partnership Instrument, AAP 2017) | 01/01/2019-31/12/2022 (mid-term) | SCGI |
| **Trade for Decent Work**  (DG TRADE,  DG INTPA) | Promote the application of ILO Fundamental Conventions under the framework of EU GSP+. Support the Government in consolidating its compliance with reporting obligations and replying to the issues raised by the Committee of the Experts on the Application of Conventions and Recommendations concerning the application of ILO Fundamental Conventions.  Promote the ILO Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy (MNE Declaration)  Focus on specific sector per country: mining in Madagascar, fish processing and tourism in Cabo Verde, cocoa and forestry in Côte d’Ivoire, cocoa in Ghana, mining sector in Mozambique. | TA grant (indirect mgnt) | Governments and social partners | Horizontal, (specific sector selected at country level) | Madagascar, Cabo Verde, Côte d’Ivoire, Ghana, Mozambique | ILO | 2020: EUR 0,9 Mio  2021: EUR 3,8 Mio including EUR 1 Mio from DG INTPA)  2022: EUR 1,5 Mio | 2020 -2022 | SCGI; GSP+; RMR; Deforestation Regulation |
| **Socieux+** | Technical assistance facility that aims at expanding and improving access to better employment opportunities and inclusive Social Protection systems in Partner Countries. It works on making employment and social protection policies, strategies and systems more inclusive, effective and sustainable.  The expected results include:  1. Institutional capacities of employment, labour and Social Protection institutions are strengthened and reinforced  2. Enhanced public capacities for improving access to employment and Social Protection is expanded to poor and vulnerable groups  3.Awareness and knowledge on Social Protection and decent work is increased | TA (Indirect mgnt) | Partner country public admin. in area of employment and social protection | horizontal | global | Expertise France in partnership with FIAPP, ENABEL and Service Public Fédéral Sécurité Sociale | EUR 11 Mio.  (total budget EUR 12,5 Mio) | July 2020 –June 2024 | SCGI |
| **Partnership for Action on Green Economy (PAGE) Phases I and II**  (DG INTPA) | The Partnership for Action on Green Economy (PAGE) is a coordinated response from five UN agencies (ILO, UNEP, UNIDO, UNITAR and UNDP) to the outcome of the United Nations Conference on Sustainable Development (Rio+20). PAGE delivers support on the basis of beneficiary countries' demand and demonstrated commitment to develop enabling policy and institutional frameworks on the inclusive green economy. | Grants | National governments | Horizontal - green economy | Africa, Asia, Latin America | UNDP, UNEP, ILO, UNIDO, UNITAR | EUR 17 Mio. | 2016-2023 | CEAP, SCGI |
| **Extractive Industries Transparency Initiative (EITI)**  (DG INTPA) | The EITI is the global standard to promote the open and accountable management of oil, gas and mineral resources. The standard requires the disclosure of information along the extractive industry value chain from the point of extraction, to how revenues make their way through the government, and how they benefit the public. By doing so, the EITI seeks to strengthen public and corporate governance, promote understanding of natural resource management, and provide the data to inform reforms for greater transparency and accountability in the extractives sector. In each of the 55 implementing countries, the EITI is supported by a coalition of government, companies, and civil society.  The EU support covers technical assistance missions (about 20 missions/year) by the EITI Secretariat to those EITI countries that are either considering implementation or are already implementing the revised 2019 EITI Standard requirements. | Co-financing grant  (Contrib. agreement to IO) | Governments of currently 55 EITI implementing countries | Textiles, minerals, handicraft | Global (EITI implemen-ting countries | EITI Secretariat based in Oslo | EUR 2,25 Mio.  (GPGC) | Since 2016 | RMR |
| **Extractives Global Programmatic Support (EGPS)**  (DG INTPA) | The EGPS is a World Bank administered Multi Donor Trust Fund that seeks to build extractives sectors in developing countries that drive inclusive, sustainable growth and development and ultimately, poverty reduction. The Trust Fund assists resource-dependent developing countries to implement a range of reforms that build a robust, transparent extractive industries sector. | Co-financing grant | Governments of resource-dependent developing countries | Minerals | Global  (resource-dependent developing countries) | World Bank | EUR 5 + 2,5 Mio. to WB SDTF | Since 2016 | RMR |
| **G7 CONNEX Initiative**  (DG INTPA) | CONNEX provides assistance to governments of developing and transitional countries in negotiating or renegotiating large-scale, complex investment contracts in the resource sector and beyond through provision of international and regional external expertise. | Co-financing grant  (Contrib. agreement to MS agency) | Partner country govern’ts | Minerals | Global (currently 16 count’s) | GIZ | ??? | Since 2020  (Prg. running since 2014) | RMR |
| **CLEAR Cotton - Eliminating child labour and forced labour in the cotton, textile and garment value chains: an integrated approach**  (DG INTPA) | The project contributes to a sustainable cotton, textile and garment supply chain that is free of child labour and forced labour by: (i) Strengthening policy, legal and regulatory frameworks to combat child labour and forced labour in the cotton, textile and garment sector; and (ii) supporting local governments, public services providers, and other relevant stakeholders to take effective action to stop child labour and forced labour in target cotton growing districts and communities and garment/textiles factories. | TA grant | Partner country govern’ts, CSOs | Textiles | Burkina Faso, Mali, Pakistan, Peru | ILO, FAO  (with sub-granting to CSOs) | EUR 7,5 Mio. | 2018-2022 | SCGI, Textiles Strategy |
| **Multi-country special measure to support the EU sustainable cocoa initiative**  (DG INTPA) | Building on the initiative by the governments of Côte d’Ivoire and Ghana to ensure a minimum price for cocoa on the world market, the overall objective is to achieve sustainable cocoa production that provides a ‘living income’ for farmers, contributes to national public revenues and end environmental degradation, including deforestation, as well as labour rights abuses including gender inequality and child labour in Côte d’Ivoire, Ghana and Cameroon. The programme will work with the public sector to strengthen the institutional, legal and regulatory frameworks for sustainable cocoa production, and with the private sector to empower cocoa value chain actors – including farmers and farmers’ cooperatives – to improve agricultural practices and comply with sustainability standards. | TA grant | Partner country governments and local producers | Agriculture – cocoa | Côte d’Ivoire, Ghana and Cameroon | JRC? | EUR 25 Mio.  (of which EUR 8 Mio. for BS; and EUR 17 Mio. for project modality) | 2021 - 2024 | SCGI, Deforestation Regulation |
| **Sustainable Supply Chains to Build Back Better – SSCBBB**  (DG EMPL) | The action aims to generate and share knowledge about the impact of COVID-19 on five supply chains, including in five countries and further tiers to help key stakeholders seize new paths and opportunities to advance decent work and build fairer, more resilient and sustainable global supply chains.  The action comprises three closely inter-related modules:  1. Analysis and research on selected supply chains, including in five countries and further tiers of the supply chains, and the impact of COVID-19;  2. Tools, policy advice and training; and  3. Support to national, sectoral, regional and global constituents and stakeholders along the five supply chains in taking action to advance decent work in the supply chains as part of their response to the COVID-19 crisis. | TA grant | Partner country govern’ts,, employers' and workers' organizations | Various (coffee, textiles, rubber gloves, electronics fisheries) | Colombia, Madagascar, Malaysia, Namibia, Vietnam | ILO | EUR 1,5 Mio.  (EU Prg. for Employment and Social Innovation - EaSI) | Jan. 2021 – March 2023 | SCGI |
| **TranspareNcy, Advocacy and Consumer Awareness raising** | | | | | | | | | |
| **Increasing Knowledge, Awareness, Transparency and Traceability for** **Responsible Value Chains in the Cotton and Garment Sectors**  (DG INTPA) | Call for proposals as part of the action “Promoting responsible value chains in the garment sector with a focus on Decent Work and Transparency/Traceability” resulting in the award of 6 grants (see separate entries) with the aim to improve working conditions, promote labour and environmental standards, reduce labour rights abuses in the cotton, and garment sector value chains.  The specific objectives of the call are (i) to improve knowledge, awareness and advocacy on social and environmental conditions to promote responsible production and consumption; and (ii) to enhance and up-scaling voluntary transparency and traceability schemes through existing multi-stakeholder initiatives to support sustainable and responsible production. | Action grants (CfP) | Stakeholders in cotton and garment sector | Textiles | Global |  | EUR 6,26 Mio.  (GPGC) | 2019-2023 | SCGI; Textiles Strategy |
| **SMART TaG - Sustainability, More Consumer Awareness, Responsibility and Transparency in the Textile and Garment Sectors**  (DG INTPA) | Grant contract awarded as part of the Call for Proposal “Increasing Knowledge, Awareness, Transparency and Traceability for Responsible VCs in the Cotton and Garment Sectors”  The project aims to improve the working conditions of garment workers, promote working and environmental standards and reduce violations of workers' rights in the textile and clothing industry, and raise awareness of consumers in Europe on sustainable consumption and production conditions in Myanmar. | Action grant (CfP) | Local businesses, EU consumers | Textiles | Myanmar | Sequa | EUR 1,35 Mio.  (80% of project costs) | May 2019 - April 2022 | SCGI, Textiles Strategy |
| **Bottom UP! Promoting a sustainable cotton & garment value chain from Ethiopian cotton to European consumers**  (DG INTPA) | Grant contract awarded as part of the Call for Proposal “Increasing Knowledge, Awareness, Transparency and Traceability for Responsible VCs in the Cotton and Garment Sectors”  The project seeks to generate business growth, improve working conditions, promote labour and environmental standards, and responsible purchasing practices in the cotton and textiles industry in Ethiopia and Europe. | Action grant (CfP) | Local businesses, EU consumers | Textiles | Ethiopia | Stichting Solidaridad Nederland | 1,5 Mio.  (78% of project costs) | 2019 – 2022 | SCGI, Textiles Strategy |
| **Filling the gap: Achieving living wages through improved transparency**  (DG INTPA) | Grant contract awarded as part of the Call for Proposal “Increasing Knowledge, Awareness, Transparency and Traceability for Responsible VCs in the Cotton and Garment Sectors” | Action grant (CfP) | Garment workers, consumers | Textiles | China, India, Indonesia | Clean Clothes Campaign | EUR 1,23 Mio (80% of project costs) | April 2019 - March 2022 | SCGI, Textiles Strategy |
| **Decent leather. Labour standards for workers in the leather-based garment, footwear and accessories value chain**  (DG INTPA) | Grant contract awarded as part of the Call for Proposal “Increasing Knowledge, Awareness, Transparency and Traceability for Responsible VCs in the Cotton and Garment Sectors”.  The project aims to improve working conditions and to reduce labour rights abuses, focusing on leather product production hubs in South Asia. It works to secure increased commitment from companies to fulfil their human rights due diligence obligations and governments to put in place safeguards and regulation to improve adherence to international labour standards. | Action grant (CfP) | Garment workers, consumers | Textiles | India, Pakistan, Bangladesh | SOMO, ARISA, BLF, Cividep India, INKOTA, Suedwind, NOW Communities | EUR 0,55 Mio (54% of project costs) | April 2020 –March 2023 | SCGI, Textiles Strategy |
| **Development Cooperation and Awareness Raising (DEAR) Programme**  (DG INTPA) | The objective of the programme is to inform and actively engage EU citizens in promoting sustainable development and addressing global challenges such as climate change and inequalities at local and global level. | Grants | EU and local CSOs | horizontal | global | EU CSOs |  | 2021-2027 | SCGI |

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1. [Commission Study on due diligence](file:///C:\Users\simicma\Downloads\DS0120017ENN.en%20(2).pdf), p. 16 [↑](#footnote-ref-2)
2. [Commission Study on due diligence](file:///C:\Users\simicma\Downloads\DS0120017ENN.en%20(2).pdf), p. 16 [↑](#footnote-ref-3)
3. As regards human rights they are advised to be linked to the International Bill of Human Rights, ILO’s Declaration on Fundamental Principles and Rights at Work and align with UNGP24 (prioritisation). [↑](#footnote-ref-4)
4. As regards environmental aspects, they are advised to be linked to Chapter VI of the OECD MNE guidelines [2011]. [↑](#footnote-ref-5)
5. [Factual summary of the open public consultation](https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12548-Sustainable-corporate-governance/public-consultation_en) [↑](#footnote-ref-6)
6. The responses were analysed in line with the requirement of Tool #54 of the Better Regulation toolbox [↑](#footnote-ref-7)
7. Among those who responded as public authority, the following Member States are represented: Belgium (3 responses), Spain (4 responses), France (2 responses) Germany (2 responses), Czechia (1 response), Denmark (1 response), Estonia (1 response), Finland (1 response), Italy (1 response), Luxembourg (1 response) and the Netherlands (1 response). Given that Denmark, Sweden and the Netherlands also submitted a position paper, in total 12 different Member States participated in this consultation. [↑](#footnote-ref-8)
8. Breakdown of responses by stakeholders groups on all the points presented below is highlighted only in case of differences in the opinions. [↑](#footnote-ref-9)
9. NGOs supported the need for a holistic approach with 93.2%, companies with 60% and business associations with 58.6% of respondents. A small group of respondents indicated that these interests should only be considered to the extent that these issues are relevant for the financial performance of the company (18.5% of those expressing an opinion). [↑](#footnote-ref-10)
10. This result is in line with the results of the survey in the [Supporting study on directors’ duties](https://op.europa.eu/en/publication-detail/-/publication/e47928a2-d20b-11ea-adf7-01aa75ed71a1/language-en), where 91% of respondents agreed with the statement that the company’s interest should encompass the interest of stakeholders and the environment other than the interests of shareholders. [↑](#footnote-ref-11)
11. NGOs supported the need for action with 95.9%, companies with 68.4% and business associations with 59.6 %. [↑](#footnote-ref-12)
12. This result is in line with the results of survey in the [Supporting study on due diligence](https://op.europa.eu/en/publication-detail/-/publication/8ba0a8fd-4c83-11ea-b8b7-01aa75ed71a1/language-en), where a large majority of stakeholders (business survey respondents (75.37%), civil society organisations (96.51%) and industry organisations (62.5%)) agreed that EU-level regulation on a general due diligence requirement for human rights and environmental impacts may provide benefits. [↑](#footnote-ref-13)
13. Individual businesses expressed slight support (a: 54.3%, b: 59.2%, c: 46.8%) while business associations expressed disagreement (a: 64.6%, b: 65.6%, c: 69.9%). NGOs, on the other hand, mostly agreed (a: 93.7%, b: 91.8%, c: 83.7%). Member States respondents mostly agreed, with 10 responses (from Belgium, Czechia, France, Germany, Luxembourg and Spain) expressing support and one respondent from France and one from Spain disagreeing to some extent. [↑](#footnote-ref-14)
14. Individual companies were acquiescent (49.4% expressing support) while business associations mostly expressed disagreement (73.9%). 93.1% of NGOs expressed support. As regards Member State responses, 8 responses (from Belgium, Czechia, France, Germany, Italy Luxembourg and Spain) agreed. One respondent from France, one from Spain and one from Italy disagreed to some extent. [↑](#footnote-ref-15)
15. While 92.4% of NGOs expressed agreement, individual companies expressed disagreement with 53.9% and business associations did so with 77.5%. As regards Member States, 7 respondents (from Belgium, Germany and Spain) agree and 5 disagree (from Finland, France, Italy, Luxembourg and Spain). [↑](#footnote-ref-16)
16. Individual companies and business associations expressed support (70.6%). In the case of NGO respondents, 92.4% agreed. As regards Member State respondents, 11 respondents agree (Belgium, France, Germany, Italy, Luxembourg and Spain), while 1 respondent from France disagrees. [↑](#footnote-ref-17)
17. NGOs expressed support (90.8%). Individual companies however expressed concern, with 68.9% expressing disagreement, while business associations expressed strong disagreement (89.8%). As regards Member State respondents, five public authority respondents from Belgium, Germany and Spain agree with the statement, whereas 4 respondents from France, Estonia, Italy and Spain disagree. [↑](#footnote-ref-18)
18. This is true also for Member States respondents. 13 respondents (from Belgium, Czechia, Estonia, Finland, France, Germany and Spain) prefer a horizontal approach. One respondent from Luxembourg prefers a thematic approach. One respondent from Italy and one from Netherlands think that none of the provided options are preferable. [↑](#footnote-ref-19)
19. It was followed by a principle-based approach (26.7%) and a minimum process and definitions approach. [↑](#footnote-ref-20)
20. It was followed by the principles-based approach (32%), and a minimum process and definitions approach complemented with further requirements in particular for environmental issues (19%). [↑](#footnote-ref-21)
21. Human rights, climate change mitigation, natural capital, and interests of local communities, indigenous peoples’ rights, and rights of vulnerable groups. [↑](#footnote-ref-22)
22. Such as International Labour Organisation (ILO) Conventions, United Nations Guiding Principles on Business and Human Rights, OECD guidelines, the Paris Agreement, etc. [↑](#footnote-ref-23)
23. All Member State respondents agree with this statement as well. The respondents who didn’t express agreement expressed their concern about the difficulty and unfeasibility of the procedure of a due diligence rule applying also to certain third country companies which are not established in the EU but carrying out certain activities in the EU. [↑](#footnote-ref-24)
24. For those who recommend that the due diligence system should apply to third country companies carrying activities in the EU, most expressed that turnover should determine whether third country companies are subject to EU legislation. To a lesser extent, other respondents think that (1) companies operating within EU borders, (2) companies with a link to the EU market, (3) companies with parts of their supply chain located or active in Europe, and (4) companies listed on EU stock markets should be subject to EU legislation. Finally, some respondents refer to other legislation to determine what link should be required (e.g. the Timber Regulation and Directive 2019/633 on Unfair Trading Practices). [↑](#footnote-ref-25)
25. As regards Member State respondents, 9 respondents from Belgium, France, Germany and Italy prefer this option, whereas 5 from Czechia, Estonia, France and Luxembourg do not. [↑](#footnote-ref-26)
26. This was followed by the option of judicial enforcement with liability (49%) and supervision by competent national authorities based on complaints about non-compliance with effective sanctions (44%). [↑](#footnote-ref-27)
27. When asked which stakeholders should be represented, the most commonly identified stakeholders were employees, either directly or through employee representatives, NGOs and CSOs, local communities, vulnerable populations, experts, harmed parties, supply chain participants and consumers. A small group of respondents indicated that all stakeholders that have a link with, or have the potential to be affected by the activities of a company, should be engaged. [↑](#footnote-ref-28)
28. When asked which mechanisms for stakeholder engagement should be promoted at the EU level, a majority of respondents expressed that complaint mechanisms as part of due diligence should be promoted at the EU level, followed by advisory bodies and stakeholder general meeting. [↑](#footnote-ref-29)
29. It is noted that, overall, approximately half of the respondents did not answer the question. Individual companies and business associations were particularly reluctant to rank options with approximately one in three providing an answer. [↑](#footnote-ref-30)
30. Those favouring the option to take workforce remuneration and related policies into account when setting directors’ remuneration, argue that the CEO-to-worker wage gap in its current evolution undermines social cohesion. Some suggest ‘the Durcker principle’, which states that corporate directors’ remuneration should never be higher than 20 times the mean salary of the company. Many respondents also highlighted the fact that there is no empirical evidence of negative consequences on the firm’s performance where this principle has been enacted, for example in the French public sector. [↑](#footnote-ref-31)
31. This is in line with results of the Supporting study on directors’ duties: “a substantial strand of literature argues that share-based remuneration of executives reinforces, rather than works against, the capital market pressure for maximisation of returns to shareholders in the short term. Share-based remuneration schemes create incentives for executives to focus on shareholder value maximisation and manage corporate resource in a way aimed to increase share price, benefiting themselves and the shareholders, at the expense of investments that are necessary for the long-term sustainability of the company”. [↑](#footnote-ref-32)
32. The second and third options were requirements for companies to consider sustainability expertise in the directors’ nomination and selection process (37,8%) and requirements for companies to have a certain number/percentage of directors with relevant sustainability expertise respectively (36,8%). [↑](#footnote-ref-33)
33. It is followed by the binding law (mean scores of 5.54, 5.16 and 4.85) and non-binding guidance (mean scores of 2.42, 1.96 and 2.15). [↑](#footnote-ref-34)
34. Mainly better environmental and social performance (mean score of 6.83) and better risk management (mean score of 6.58) are expected. Benefits of binding law are scored a little lower, but show the same pattern. Benefits of non-binding law are rated lowest. [↑](#footnote-ref-35)
35. Costs of non-binding guidance are rated the highest by EU citizens and consumer organisations (mean is 8.83), followed by company/business organisations and business associations (mean is 6.26) and NGOs and environmental organisations (mean is 5.63). Trade unions rate costs extremely low (mean is 0.60). Costs of binding law are rated the highest by NGOs and environmental organisations (mean is 18.11), followed by company/business organisations (mean is 17.23) and EU citizens and consumer organisations (mean is 12.61). Again, trade unions rate costs very low (mean is 1.60). [↑](#footnote-ref-36)
36. Benefits of non-binding guidance are rated the highest by EU citizens and consumer organisations (mean is 26.18), followed by NGOs and environmental organisations (mean is 21.50) and company/business organisations and business associations (mean is 19.55). Trade unions score these benefits relatively low with a mean rating of 5.00. On the contrary, trade unions rate benefits related to binding law (mean is 25.00) higher than companies/business organisations and business associations (mean is 22.50). EU citizens and consumer organisations rate these benefits the highest with a mean rating of 30.20, followed by NGOs and environmental organisations (mean is 22.50). [↑](#footnote-ref-37)
37. In the 1980s, Boliden paid Promel to export industrial waste to Chile, where Promel disposed of it without removing the arsenic. This caused awful health effects, including cancers and neurological disorders, for people living near the site. In 2013 victims took legal action against Boliden in the Swedish courts arguing that Boliden had breached a duty to ensure that the sludge was appropriately processed by Promel, but eventually lost their case. In March 2019, after the claimants appealed, the court decided to apply Swedish law and dismissed the appeal on the basis that the claim for damages had been filed too late and the cause of action was time-barred. Boliden has not faced legal consequences for this negligence. [↑](#footnote-ref-38)
38. On 11 September 2012, 258 workers died and hundreds were seriously injured when a fire broke out in the Ali Enterprise garment factory in Karachi, Pakistan. Due to lax fire safety measures, workers were at first unaware of and then trapped by the fire. At the time, the factory was producing jeans for its main client, German retailer KiK. Victims sought justice in the German courts, but the court decided to apply Pakistani law, as this was where the harm occurred, and dismissed the action, deciding that according to Pakistani law the statute of limitation had expired and the claimants were too late to seek justice. [↑](#footnote-ref-39)
39. According to reports, Shell is ravaging the Niger Delta through its decades-long quest for oil. Pollution caused by the activities of its subsidiary SPDC is having a devastating effect on both the ecosystem and people living in this area. Victims of Shell’s conduct sued the company before Dutch courts, but claimants have faced legal barriers, challenges and uncertainty. The case is not closed yet. The story has exposed the weakness of current EU law in allowing victims of corporate harm effective access to remedy and justice. [↑](#footnote-ref-40)
40. 1 = Requirement for the board to regularly assess its level of expertise on environmental, social and/or human rights matters and take appropriate follow-up, including regular trainings.

    2 = Requirement for companies to consider environmental, social and/or human rights expertise in the directors’ nomination and selection process.

    3 = Requirement for companies to have a certain number/percentage of directors with relevant environmental, social and/or human rights expertise.

    4 = Requirement for companies to have at least one director with relevant environmental, social and/or human rights expertise. [↑](#footnote-ref-41)
41. For instance academic contributions concerning the Study on directors duties from [ECLE (The European Company Law Experts Group)](https://www.law.ox.ac.uk/business-law-blog/blog/2020/12/ec-corporate-governance-initiative-series-comment-european-company); [Bassen, A./Lopatta, K./Ringe W.-G. “The EU Sustainable Corporate Governance Initiative – room for improvement”(15 October 2020)](https://www.law.ox.ac.uk/business-law-blog/blog/2020/10/ec-corporate-governance-initiative-series-eu-sustainable-corporate) ; [Andersen, P. K./Bergthorsson, A./Bråthen, T./Hansen, S. F./Hansen, J. L./Johansson, S./Kinander, M./Knuts, M./Lidman, E./Lilja, T. M./Skovmand Rasmussen, N. /Sillanpää, M. J./Skog, R. R./Stattin, D./Strand, T./Villa, S./Rose, C./Samuelsson, P./Sjöberg, G./Vahtera, V./Werlauff, E., “Response to the Study on Directors’ Duties and Sustainable Corporate Governance by Nordic Company Law Scholars” (October 7, 2020)](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3709762); [Roe, Mark/Spamann, Holger/Fried, Jesse/Wang, Charles “A Critique of the Sustainable Corporate Governance Report from the European Commission” (9 November 2020)](https://clsbluesky.law.columbia.edu/2020/11/09/the-european-commissions-sustainable-corporate-governance-report-a-critique/). See also [Edmans, Alex/Enriques, Luca/Thomsen, Steen “Call for Reflection on Sustainable Corporate Governance” (9 April 2021)](https://www.law.ox.ac.uk/business-law-blog/blog/2021/04/ec-corporate-governance-initiative-series-call-reflection-sustainable). [↑](#footnote-ref-42)
42. Confederation of Finnish Industries, Business Europe, Bulgarian Industrial Capital Association, European Community Shipowners’ Associations, Confederation of Industry and Transport of Czechia, SGI Europe, Union des Entreprises de Proximité, SMEunited, European Chemical Employers Group, Confederation of German Employers' Associations, Federation of Austrian Industries, Eurochambers, ABIRD, Confederation of Netherlands Industry and Employers, Confederation of Swedish Enterprise, European Tech & Industry Employers, Wirtschaftskammer Österreich, European Apparel and Textile Confederation, MEDEF, Confederation of Danish Employers. [↑](#footnote-ref-43)
43. Central Organisation of Finnish Trade unions, Italian General Confederation of Labour, General Union of Workers, ETUC, European Transport Workers' Federation, Workers Commissions, Confederation of Independent Trade Unions of Bulgaria, Swedish Confederation of Professional Employees, European Federation of Public Service Unions, Austrian Trade Union Federation, IndustriAll, Confédération française démocratique du travail, Italian Confederation of Workers’ trade unions, Force ouvrière, UNI Europa, European Federation of Trade Unions in the Food, Agriculture and Tourism, European Confederation of Police, German Trade Union Confederation. [↑](#footnote-ref-44)
44. DE, SE, EE, IT, FR, NL, FI, DK, LU, AT expressed support for the initiative to introduce mandatory due diligence legislation. [↑](#footnote-ref-45)
45. E.g. EE, FR, DK suggested initially extending mandatory due diligence to large companies only. IT saw the need for including SMEs active in high-risk sectors while LU considered that excluding SMEs would diminish the effectiveness. [↑](#footnote-ref-46)
46. E.g. EE, DK, SE considered that there is no need to introduce legislation on directors’ duties and recommended to separate the part of the initiative on directors’ duties from the part on due diligence. DE welcomed the part of the initiative on directors’ duties but was hesitant when it comes to harmonising enforcement of the duty against directors. FR expressed agreement with a principles-based approach whereby directors are legally obliged to act in the company interest. [↑](#footnote-ref-47)
47. Shift collected 24 business model red flags to help the identification of risks to people that may be embedded in the business model of a company. These concern 3 different features of business models: (i) what the company offers and to whom, (ii) the value chain and (iii) the cost structure and revenue model of the company. The red flags include, for instance, business models built on or involving: the provision of the lowest cost goods, high-speed delivery that places pressure on warehouse workers, land use in countries where ownership rights may be contested, depleting natural resources that are key for access or health, sourcing of commodities priced independently from farmers’ income, or operating in markets with low human rights standards. See [Menu of Red Flags - Shift (shiftproject.org)](https://shiftproject.org/resource/business-model-red-flags/menu-of-red-flags/) [↑](#footnote-ref-48)
48. SWD (2017) 350, in particular [Chapter III: Guidelines on Impact Assessment](https://ec.europa.eu/info/sites/info/files/better-regulation-guidelines-impact-assessment.pdf). [↑](#footnote-ref-49)
49. Literature relevant for our assessment is growing every day. New data and analyses are published not only pointing to urgency and significance of the problems, but also on the impacts of the possible tools that could tackle them. However, there are obvious limitations to considering all recently published assessments in this assessment. [↑](#footnote-ref-50)
50. E.g. the various potential benefits for the businesses often move jointly or even have a multi-causal relationship with each other, or, regarding cost elements, it is likely that the more a company invests in compliance and the transition to sustainability, the less litigation it will face. [↑](#footnote-ref-51)
51. See Supporting Study on Due Diligence, p. 301 and the lists of studies in Annexure IV, Tables 8, 9, 11. [↑](#footnote-ref-52)
52. See Annex C of the OECD report on [Quantifying the Costs, Benefits and Risks of Due Diligence for Responsible Business Conduct, Framework and Assessment Tool for Companies](https://mneguidelines.oecd.org/Quantifying-the-Cost-Benefits-Risks-of-Due-Diligence-for-RBC.pdf), June 2016. [↑](#footnote-ref-53)
53. According to the study, 88% of reviewed sources found that companies with robust sustainability practices demonstrated better operational performance, which ultimately translated into cashflows. See Clark, Feiner and Viehs (2015): [From the Stockholder to the Stakeholder: How Sustainability Can Drive Financial Outperformance](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2508281). [↑](#footnote-ref-54)
54. See Friede, Busch and Bassen (2015) “[ESG and financial performance: aggregated evidence from more than 2000 empirical studies](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2699610)”. [↑](#footnote-ref-55)
55. See [ESG AND FINANCIAL PERFORMANCE: Uncovering the Relationship by Aggregating Evidence from 1,000 Plus Studies Published between 2015 – 2020](https://www.stern.nyu.edu/sites/default/files/assets/documents/NYU-RAM_ESG-Paper_2021%20Rev_0.pdf) By Tensie Whelan, Ulrich Atz, Tracy Van Holt and Casey Clark, CFA. [↑](#footnote-ref-56)
56. On ESG investment, the meta-study found that 59% of the studies showed a similar or better performance relative to conventional investment approaches, while only 14% found negative results. [↑](#footnote-ref-57)
57. The authors of the above-mentioned meta-study undertook an additional meta-meta-analysis (a study of existing meta-studies published since 2015), too. The corporate meta-analysis studies were consistent on the positive ESG-CFP correlations, while the 2 investor meta-analysis studies assessed found that ESG investing returns were generally indistinguishable from conventional investing returns. These two findings were found to be robust across time and space. [↑](#footnote-ref-58)
58. See [From the Stockholder to the Stakeholder: How Sustainability Can Drive Financial Outperformance](https://ssrn.com/abstract=2508281) [↑](#footnote-ref-59)
59. Margolis, J. et al. (2009). Does it Pay to Be Good. And Does it Matter? A Meta-Analysis of the Relationship between Corporate Social and Financial Performance. [↑](#footnote-ref-60)
60. Study on due diligence, p. 450 and p. 465. [↑](#footnote-ref-61)
61. Study on due diligence, p. 466. [↑](#footnote-ref-62)
62. Edmans, A., Does the stock market fully value intangibles? Employee satisfaction and equity prices, 2011. [↑](#footnote-ref-63)
63. Edmans, A., 2011, *ibid*. [↑](#footnote-ref-64)
64. Krueger, Metzger and Wu in “[The Sustainability Wage Gap (December 17, 2020)](https://ssrn.com/abstract=3672492%20or%20http:/dx.doi.org/10.2139/ssrn.3672492)” show that wages – in particular of highly-skilled employees – can be 10% lower in firms that operate in environmentally more sustainable sectors. [↑](#footnote-ref-65)
65. Évaluation de la mise en œuvre de la loi n° 2017-399 du 27 mars 2017 relative au devoir de vigilance des sociétés mères et des entreprises donneuses d’ordre, rapport de Anne Duthilleul et Matthias de Jouvenel [↑](#footnote-ref-66)
66. See Clark, Feiner and Viehs (2015). [↑](#footnote-ref-67)
67. Study on due diligence, p. 452. [↑](#footnote-ref-68)
68. Bliss, R. and Jordan, S. and Rochlin, S. and Yaffe Kiser, C. (2015). [Project ROI Report: Defining the Competitive and Financial Advantages of Corporate Responsibility and Sustainability.](https://www.ywcasandiego.org/wp-content/uploads/Project-ROI-Report-Impact-ROI.pdf) This is a meta-analysis of 300 academic and other studies, complemented by interviews, on the benefits of managing corporate responsibility practices (incl. having strong stakeholder relationships). Among others, it shows the potential of reducing the cost of equity by 1%, increasing market value by up to: 4-6%, reducing share price volatility by 2-10%, reducing systematic risk (of a portfolio) by 4% etc. [↑](#footnote-ref-69)
69. The study looked at the initial stock market reaction to the COVID-19 crisis (up to 23 March 2020). See Cheema-Fox et al., 2020, *op. cit.*, [Corporate Resilience and Response During COVID-19](https://www.hbs.edu/ris/Publication%20Files/20-108_6f241583-89ac-4d2f-b5ba-a78a4a17babb.pdf), Harvard Business School Working Paper 20-108. [↑](#footnote-ref-70)
70. Note prepared by the OECD Centre for Responsible Business Conduct “[COVID 19 and Responsible Business Conduct](https://read.oecd-ilibrary.org/view/?ref=129_129619-6upr496iui&title=COVID-19-and-responsible-business-conduct)”. [↑](#footnote-ref-71)
71. European Capital Markets Institute [*ESG resilience during the Covid crisis: Is green the new gold?*](https://www.ecmi.eu/sites/default/files/ecmi_commentary_no_67_july_2020.pdf)July 2020 [↑](#footnote-ref-72)
72. World Economic Forum (2019), ‘[The Global Risks Report](https://www.weforum.org/reports/the-global-risks-report-2019)’, 14th Edition, World Economic Forum, Geneva. [↑](#footnote-ref-73)
73. WBCSD/COSO (2018), ‘Applying Enterprise Risk Management to Environmental, Social and Governance-related Risks’. [↑](#footnote-ref-74)
74. Sassen, R.; Hinze, A.K.; Hardeck, I. (2016). Impact of ESG factors on firm risk in Europe. Journal of Business Economics, Volume 86, Issue 8, pp 867–904, also referred to in the Supporting study on due diligence, p. 451. [↑](#footnote-ref-75)
75. As referred to in the Supporting study on due diligence, p. 314 [↑](#footnote-ref-76)
76. See [ESG AND FINANCIAL PERFORMANCE: Uncovering the Relationship by Aggregating Evidence from 1,000 Plus Studies Published between 2015 – 2020](https://www.stern.nyu.edu/sites/default/files/assets/documents/NYU-RAM_ESG-Paper_2021%20Rev_0.pdf) by Tensie Whelan, Ulrich Atz, Tracy Van Holt and Casey Clark, CFA, referred to above. [↑](#footnote-ref-77)
77. See note prepared by the OECD Centre for Responsible Business Conduct “[COVID 19 and Responsible Business Conduct](https://read.oecd-ilibrary.org/view/?ref=129_129619-6upr496iui&title=COVID-19-and-responsible-business-conduct)”. [↑](#footnote-ref-78)
78. See more studies on the COVID-19 crisis under the point on “stock price” and in Annex 14. [↑](#footnote-ref-79)
79. See e.g. N. C. Ashwin Kumar, Camille Smith, Leïla Badis, Nan Wang, Paz Ambrosy and Rodrigo Tavares (2016): ESG factors and risk-adjusted performance: a new quantitative model. Also see Ameer, R. and Othman, R. (2012). Sustainability Practices and Corporate Financial Performance: A Study Based on the Top Global Corporations. This assessment of top sustainable companies shows significantly higher sales growth, return on assets, profit, and cash flows from operations in some activity sectors. [↑](#footnote-ref-80)
80. Supporting study on due diligence, p. 315. [↑](#footnote-ref-81)
81. Supporting study on due diligence, p. 315 and Annexure IV, table 12 p. 81 [↑](#footnote-ref-82)
82. Supporting study on due diligence, p. 315. [↑](#footnote-ref-83)
83. McKinsey (2017) [Sustainability’s deepening imprint](https://www.mckinsey.com/business-functions/sustainability/our-insights/sustainabilitys-deepening-imprint) and Supporting study on due diligence, p. 315 [↑](#footnote-ref-84)
84. Capozucca, P. and Sarni, W. (2012). [Sustainability 2.0 - Using sustainability to drive business innovation and growth](https://www2.deloitte.com/us/en/insights/deloitte-review/issue-10/sustainability-2-0-innovation-and-growth-through-sustainability.html). [↑](#footnote-ref-85)
85. Supporting study on due diligence, p. 445. [↑](#footnote-ref-86)
86. [Six business benefits of setting science-based targets](https://sciencebasedtargets.org/blog/six-business-benefits-of-setting-science-based-targets) by Dexter Galvin, Global Director of Corporates and Supply Chains, CDP (2018). [↑](#footnote-ref-87)
87. See also Clark, Gordon L. and Feiner, Andreas and Viehs, Michael, “[From the Stockholder to the Stakeholder: How Sustainability Can Drive Financial Outperformance](https://ssrn.com/abstract=2508281)” (2015). [↑](#footnote-ref-88)
88. Supporting study on due diligence, p. 173. [↑](#footnote-ref-89)
89. Évaluation de la mise en œuvre de la loi n° 2017-399 du 27 mars 2017 relative au devoir de vigilance des sociétés mères et des entreprises donneuses d’ordre, rapport de Anne Duthilleul et Matthias de Jouvenel. [↑](#footnote-ref-90)
90. See more in the Supporting study on due diligence, p. 387 and p.398. Tables 1 to 7 of Annexure D of the study collects the estimates for the various costs elements assessed for relevant policy initiatives. [↑](#footnote-ref-91)
91. For more information on the development of the survey and the sample see pages 44 and 401-402 of the study. [↑](#footnote-ref-92)
92. Monthly person-day estimates are multiplied by the calculated EU average daily labour cost (using an 8-hour working day and the hourly labour costs of EUR 27.40 which is based on Eurostat data for 2018) and are annualised. [↑](#footnote-ref-93)
93. The authors found the data on person-days to be more consistent and reliable. Nevertheless, they added the above-mentioned mark-ups for the selected two cost types as those were found to be significant in proportion to the total costs. For the mark-ups, see pages 415 and 429 of the Supporting study. [↑](#footnote-ref-94)
94. Also, lack of benefit of court judgments even where due diligence laws already existed resulted in varying expectations among the respondents with regard to the legal obligations and the relevant corporate activities necessary to comply with these obligations. See more on the limitations of the assessment in the study, p. 398-400. [↑](#footnote-ref-95)
95. As regards experience with due diligence, **30% of the very large companies (with 1000 employees or more)** participating in the surveyreported that they were already undertaking “human rights due diligence which takes into account all human rights (including environment)”, and **an additional 31%** reported to have already conducted due diligence limited to certain areas (out of which 4% state to conduct specifically environmental or climate change due diligence). This contrasts with **middle-ground and medium-sized companies (with 50-1000 employees)** which tend to have less experience with due diligence: **only 18%** of them reported that they have already conducted corporate due diligence across the full spectrum of possible adverse impacts, and **15%** reported to have already undertaken due diligence limited to certain areas.

    **Small** companies (with less than 50 employees) generally do not conduct any due diligence activities.

    Overall, only 4% of the respondents stated that their companies did not yet undertake any form of due diligence activities, the rest did not indicate or did not know whether their companies already conducted certain due diligence activities. [↑](#footnote-ref-96)
96. It appears that comprehensive costs estimates were received from about 50 companies. [↑](#footnote-ref-97)
97. About 30 companies fall in this category. However, not all of them provided estimates for all scenarios. [↑](#footnote-ref-98)
98. **More than half of the participants in the overall survey represented very large companies with 1000 employees or more**, and only 18% represented companies with more than 50 but less than 1 000 employees. Within this category, companies with 50 to 250 (medium-sized companies), 250 to 500 and 500 to 1000 employees were almost equally represented (5 to 7%). 8% were small companies with less than 50 employees, 22% did not indicate their sizes.

    180 business respondents to the overall questionnaire (of which about 69% had more than 1000 employees) reported estimates for their companies’ **total annual turnover: 25% had less than EUR 213.5 million**, 50% had less than 5.55 billion, while 25% reported more than 21.75 billion, with the highest turnover reported EUR 210 billion. [↑](#footnote-ref-99)
99. Within this group, the **median revenue** of those providing both person-day estimates and revenue data is **EUR 11.5 billion**. The median revenue for the group of experienced smaller companies (with 50 to 1000 employees) is substantially lower: EUR 128 million. [↑](#footnote-ref-100)
100. In search for more relevant data after the policy options of this initiative have been outlined more precisely, we checked the **raw data** of the survey and found that data from companies with less than 1000 employees that already have at least some experience with conducting full human rights and environmental due diligence **are still too few and too scattered** to draw any far-reaching conclusions. [↑](#footnote-ref-101)
101. Based on pages 429-430 of the Supporting study and Table 8.35 (rounded). [↑](#footnote-ref-102)
102. Also, the study notes that **fragmentation-related costs** companies would face if national laws were adopted without EU level harmonisation are not considered either in the baseline. This can be taken into account as a possible benefit of EU regulation. [↑](#footnote-ref-103)
103. At the same time, the cost of **incorporating standards** into contracts or agreeing on a suppliers’ code of conduct, which was assessed as a recurring cost, seem to be relevant rather on the short run (**one-off cost**) when existing contract and supplier relationships need to be revised in larger number. [↑](#footnote-ref-104)
104. Nevertheless, the cost of **exercising leverage** over suppliers could also be regarded as a part of the cost of changing the companies’ value chains (**transition costs**). [↑](#footnote-ref-105)
105. Due to its recent nature, we did not use data from the German impact assessment for the detailed calculations of compliance costs, only for putting our calculations in context. [↑](#footnote-ref-106)
106. There are also **multi-stakeholder instruments**, like the Dutch [International Responsible Business Conduct Agreement for the Metals Sector](https://www.imvoconvenanten.nl/en/metals-sector/convenant), which was signed by companies, industry associations, trade unions, non-governmental organisations and the government of the Netherlands, to collectively identify and address adverse environmental and human rights impacts in the entire metal supply chain and increase collective leverage. [↑](#footnote-ref-107)
107. Section 1502 of the Dodd-Frank Act is the “conflict minerals” provision of the US. It requires US publicly-listed companies to report on the measures taken to exercise due diligence to make sure they are not funding armed groups or human rights abuses if they are sourcing minerals (tin, tungsten, tantalum and gold) from the Democratic Republic of the Congo or its neighbouring countries. [↑](#footnote-ref-108)
108. For instance, an international RBC [agreement for the European wind energy sector](https://www.imvoconvenanten.nl/en/wind-energy) was being prepared at the time of writing to identify, prevent and address risks to people and the environment across the entire wind industry’s value chain, from risks related the extraction of raw materials through the decommissioning of wind farms. [↑](#footnote-ref-109)
109. Blome, C. 2016. [Stopping Conflict Minerals with OECD Guidance for Mineral Supply Chain](http://sro.sussex.ac.uk/id/eprint/65452/1/__smbhome.uscs.susx.ac.uk_tjk30_Documents_BlomeHofmannSchleper%20-%20Stopping%20conflict%20minerals%20with%20the%20OECD%20guidance%20for%20responsible%20mineral%20supply%20chains.pdf), University of Sussex, School of Business, Management and Economics (Table 2). [↑](#footnote-ref-110)
110. For instance, PET bottles are used by the textile industry, or cement production will help recycle wind turbine blades. The chemical industry plays an important role in the transition to a circular economy by investing in the research and development of new materials but innovation is also facilitated by the collaboration of the sectors affected. [↑](#footnote-ref-111)
111. See Supporting study on due diligence, p. 445, also referring to other relevant studies. It is to be noted that these two categories of cost mitigation factors are not distinct as technological development can enable cost sharing, and the cooperation of the various actors concerned can also prompt technological innovation. [↑](#footnote-ref-112)
112. See Study prepared for the European Commission (2015) on [Traceability across the Value Chain – Advance tracking systems](https://ec.europa.eu/docsroom/documents/13393/attachments/2/translations/en/renditions/native), also referred to in the Supporting study. [↑](#footnote-ref-113)
113. <https://opentrustfabric.org/otf-at-endorse-event-2/>. [↑](#footnote-ref-114)
114. <https://www.copernicus.eu/en>. [↑](#footnote-ref-115)
115. <https://www.airbus.com/newsroom/stories/starling.html>. [↑](#footnote-ref-116)
116. This requires setting up the necessary processes, procedures, systems and organisational structures or functions (where not in place yet), hiring and training staff, it may involve conducting investigations and internal or external audit of the supply and value chains for human rights and environmental issues, and it may also include engagement with relevant stakeholders, operating early-warning and grievance mechanisms, as well as internal reporting. [↑](#footnote-ref-117)
117. Also, experience with the French law shows that complying with the law (i.e. preparing a proper risk mapping, implementing mitigation measures) is not immediate and in practice may spread across several years. See « Evaluation de la mise en œuvre de la loi n° 2017-399 du 27 mars 2017 relative au devoir de vigilance des sociétés mères et des entreprises donneuses d’ordre », rapport de Anne Duthilleul et Matthias de Jouvenel. [↑](#footnote-ref-118)
118. These are in particular the costs of incorporating sustainability standards into contracts, agreeing on a code of conduct with suppliers, building and exercising leverage (possibly jointly with others in the industry). [↑](#footnote-ref-119)
119. See [Le radar du devoir de vigilance](https://plan-vigilance.org/wp-content/uploads/2021/07/A4-VF-FICHES-FR-020721-V3.pdf) (July 2021). [↑](#footnote-ref-120)
120. Compensation (just like fines and sanctions) in case a company is found to not have been complying with its legal obligations should not be regarded as costs implied by this initiative. [↑](#footnote-ref-121)
121. The exact definition of large depends on the policy options assessed. [↑](#footnote-ref-122)
122. See CSRD impact assessment, p. 210. [↑](#footnote-ref-123)
123. The estimation of the Study for the entire SME size category also rely on data received from large companies (up to 1000 employees), thus, using the highest tranche could result in disproportionately high cost estimates. The structural break in the estimates also suggests that using the highest value indicated for SMEs would be counterintuitive. Also, our own calculations with the very few raw data available for SMEs confirm that total compliance costs for these companies could be even lower. However, we find that using a much smaller estimate (EUR 13 850) linked to the lower revenue tranche of EUR 10 million would result in the opposite distortions. [↑](#footnote-ref-124)
124. At the same time, only a few survey respondents declared that their companies were not undertaking due diligence, others either did not indicate or declared that they did not know. [↑](#footnote-ref-125)
125. E.g. compared to the BAU of around 50% in CEPS NFRD study. [↑](#footnote-ref-126)
126. The BAU factor, according to the CEPS study, is hardly affected by the type of activity of data gathering, data analysis and reporting. For the due diligence activities, this is likely to be different but, for the sake of simplification, we use a single “reverse BAU” factor for all activities. [↑](#footnote-ref-127)
127. Other administrative activities that are needed for the reporting are also undertaken to comply with the substantive obligation of this initiative and are as such only counted as substantive costs. [↑](#footnote-ref-128)
128. The most reliable estimates were given by large companies with more than 1000 employees and that already have more experience with undertaking human rights and environmental due diligence. These figures are based on the responses of 7 such companies that gave per-activity estimates for the “mandatory due diligence” scenario. [↑](#footnote-ref-129)
129. We also assume that the additional 25% overhead costs and the additional 25% cost of external services (external audits, trainings, legal experts etc.) are proportionately distributed among the various activities. [↑](#footnote-ref-130)
130. As the CSRD would also require disclosing information on corporate stakeholders, strategy, etc., CSRD-implied administrative costs will cover already part of the **compliance costs with the directors’ duties**, too. [↑](#footnote-ref-131)
131. Under the CSRD these are regarded as administrative costs related to public reporting, under this initiative they are regarded as substantive costs. [↑](#footnote-ref-132)
132. CEPS 2020 study on the NFRD review (p. 68.), also referred to in the CSRD Impact Assessment (p. 212). [↑](#footnote-ref-133)
133. While reasonable assurance of sustainability information could overlap with the cost of external audits conducted over the value chain, the CSRD proposal contains limited assurance requirement. [↑](#footnote-ref-134)
134. This middle category was used for the majority of the companies under the scope of the CSRD proposal and was calculated using the cost estimate for the lower tranche of the sample (with an average turnover of EUR 658 million). [↑](#footnote-ref-135)
135. Using the average cost estimate including the entire sample of companies, which had an average turnover of EUR 8 billion. [↑](#footnote-ref-136)
136. These activities were included in the survey conducted for the Supporting study on due diligence. Survey respondents were not requested to estimate the person-days or costs of stakeholder engagement activities. Even though the policy options assessed for this initiative in detail also foresee stakeholder engagement in the value chain, these efforts (and thus costs) are already accounted for in the various other steps as it is also an integral part of the due diligence process (during the gathering of information, exercising leverage, etc.). Therefore, we do not need to adjust the estimations to include a separate cost category on stakeholder engagement. [↑](#footnote-ref-137)
137. I.e. by using the ratio of the given activity in the total person-days calculated based on the average of the most reliable estimates received in the survey of the Supporting study on due diligence (using raw data), as explained above at the calculations regarding reporting costs. [↑](#footnote-ref-138)
138. Note that we clustered the relevant data gathering and analysis cost elements into one category to allow for comparison with the CSRD. [↑](#footnote-ref-139)
139. Porter and van der Linde, The Journal of Economic Perspectives, Toward a New Conception of the Environmental Competitiveness, 1995 [↑](#footnote-ref-140)
140. [The Sixth Carbon Budget – The UK's path to Net Zero](https://www.theccc.org.uk/wp-content/uploads/2020/12/The-Sixth-Carbon-Budget-The-UKs-path-to-Net-Zero.pdf), Committee on Climate Change (December 2020), figure 3. According to the report, by 2050.

     See also Clark, Gordon L. and Feiner, Andreas and Viehs, Michael, “[From the Stockholder to the Stakeholder: How Sustainability Can Drive Financial Outperformance](https://ssrn.com/abstract=2508281)” (2015).

     See also CDP Europe’s study: [Doubling down Europe's low carbon investment opportunity (February 2020](https://www.cdp.net/en/research/global-reports/doubling-down)) covering 882 European companies, according to which emissions reduction initiatives typically yield cost savings in excess of the initial investment at an average profit of EUR 17 per tonne of CO2. [↑](#footnote-ref-141)
141. As an example, ENEL plans to invest EUR 16.8 billion in onshore wind and solar by 2023, promising to raise core earnings by 13%. Please refer to Annex 4 for more details on how the cost of transition to zero-emissions is decreasing and how low-carbon investments are becoming profitable. [↑](#footnote-ref-142)
142. See the literature review above [↑](#footnote-ref-143)
143. This also explains why we do not calculate with additional compliance costs (other than the one-off fee for science-based target setting services and the related administrative costs) for companies that are required to mitigate their negative climate and relevant environmental impacts in line with science-based targets. [↑](#footnote-ref-144)
144. The world already lost an estimated €3.5-18.5 trillion per year in ecosystem services from 1997 to 2011, and an estimated €5.5-10.5 trillion per year from land degradation (Fact sheet on nature and biodiversity, European Commission Nov 2020.) [↑](#footnote-ref-145)
145. Environmental topics such as pollution abatement, resource efficiency and corporate environmental management practices in general are often mentioned as the most relevant to operational performance (OECD report, Annex C p. 39). Relative resource efficiency (the amount of energy, water, and waste used in relation to revenue) is significantly correlated (95-99% confidence) with financial performance in sectors as diverse as food products, specialty chemicals, pharmaceuticals, automotive, and semiconductors. (See Annexure IV of Supporting study on due diligence, p. 81, Table 13, rows 2 and 3). [↑](#footnote-ref-146)
146. Clark, Gordon L. and Feiner, Andreas and Viehs, Michael, “[From the Stockholder to the Stakeholder: How Sustainability Can Drive Financial Outperformance](https://ssrn.com/abstract=2508281%20or%20http:/dx.doi.org/10.2139/ssrn.2508281)” (March 5, 2015). [↑](#footnote-ref-147)
147. [Doubling down Europe's low carbon investment opportunity, February 2020](https://www.cdp.net/en/research/global-reports/doubling-down) [↑](#footnote-ref-148)
148. While the companies anticipated more than 2.4 GtCO2e of cumulative emissions reductions over the lifetime of their initiatives – more than the annual emissions of Germany, the United Kingdom, Italy, Poland and France combined –, they also expected to achieve €65 billion of cost savings over the lifetimes of their investments. Compared to their initial €24 billion of investments (in 2019) this represents a net €41 billion contribution to bottom line. [↑](#footnote-ref-149)
149. The most profitable emissions reduction initiatives were expected to be investments in energy efficiency processes but significant abatement profits were also anticipated from investments in transport electrification and low-carbon energy. [↑](#footnote-ref-150)
150. See [How Enel became Europe’s climate centurion | The Economist](https://www.economist.com/business/2020/11/28/how-enel-became-europes-climate-centurion), 28 November 2020. [↑](#footnote-ref-151)
151. For simplified due diligence, which applies under certain options mainly to medium-sized companies, a 25% discount was estimated compared to these data. [↑](#footnote-ref-152)
152. For the majority of large companies the lower estimate is relevant, the larger values only concern about 300 very large companies. [↑](#footnote-ref-153)
153. In the case of SMEs, the smaller estimates concern companies that fall under the scope of the CSRD. [↑](#footnote-ref-154)
154. This is the cost of **third-party assurance of the non-financial (sustainability) reporting** which, depending on the level of assurance agreed upon, can cover all of the content of the non-financial statements (including key performance indicators, processes and the report) or be limited to e.g. a selection of KPIs or to checking the processes leading to the reported figures. Reasonable assurance of the report is estimated to cost EUR 26 870 annually. [↑](#footnote-ref-155)
155. Reasonable assurance of report would cost EUR 125 000 annually for very large companies with EUR 8 billion average turnover, and EUR 57 000 for large companies with average turnover of EUR 658 million. [↑](#footnote-ref-156)
156. The Supporting study on due diligence seems to use a more granular approach for aggregating the costs in the case of SMEs but only one size category for the large companies, in accordance with the availability of corporate revenue data for companies with 1-19, 20-49, 50-249 and 250 or more employees (see Part IV: Annex

     ures, Table 0.2). As the policy options assessed in detail in this report cover small companies only in case they are listed, and because the costs are substantially higher for companies with very high revenues, our calculations are **more granular in the large company size group.** [↑](#footnote-ref-157)
157. Annex 11 contains **the number of midcaps and medium-sized companies** (according to the two different definitions) operating in the identified high-impact sectors, **excluding those** that should not be subject to a simplified duty as they **belong to the group or value chain of a larger company which is subject to the full regime**, covering all impact types (and extending to subsidiaries and value chains). As explained in that annex, the correction factor is estimated to be about 50%. [↑](#footnote-ref-158)
158. To simplify the calculations we assumed that not more than 10% of the large companies have a turnover exceeding EUR 5 billion. [↑](#footnote-ref-159)
159. This separation is only made for calculating the cost which are, at firm level, different for the large and for the medium-sized companies. Overall, the scope covers all medium-sized and large companies, i.e. all LLCs with a minimum of 50 employees and a minimum of EUR 8 million turnover. [↑](#footnote-ref-160)
160. Assuming that in this sector 10% of the large companies have more than EUR 5 billion turnover. [↑](#footnote-ref-161)
161. Calculated with 40% of the estimated costs of simplified due diligence obligation that would target the most relevant issues. [↑](#footnote-ref-162)
162. For relevant reserch, see Arabesque, From stockholder to stakeholder. [↑](#footnote-ref-163)
163. Eccles and Serafeim, 2013, Harvard Business Review, The Performance Frontier. [↑](#footnote-ref-164)
164. At the same time, the averages used in the study overestimate firm-level annual costs as shown in the previous sections (due to the lack of accounting for the evolution of the dynamic baseline, for cost mitigating factors etc.). [↑](#footnote-ref-165)
165. Évaluation de la mise en œuvre de la loi n° 2017-399 du 27 mars 2017 relative au devoir de vigilance des sociétés mères et des entreprises donneuses d’ordre, rapport de Anne Duthilleul et Matthias de Jouvenel. [↑](#footnote-ref-166)
166. See the justification of the bill submitted by the government: [Referentenentwurf](https://www.bmas.de/SharedDocs/Downloads/DE/Gesetze/Regierungsentwuerfe/reg-sorgfaltspflichtengesetz.pdf?__blob=publicationFile&v=1) des Bundesministeriums für Arbeit und Soziales Gesetz über die unternehmerischen Sorgfaltspflichten in Lieferketten, adopted by the Federal Government of Germany on 3 March 2021. [↑](#footnote-ref-167)
167. The costs in the German calculations refer only to very large companies that have more than 3000 employees. [↑](#footnote-ref-168)
168. This will result in a weighted „efficiency” rate for the total group of supervised companies as follows: 20% x (number of SMEs / total number of companies) +100% x (number of large companies / total number of companies) for all supervisory activities, except for training (which is calculated per Member State, for the sake of simplification). [↑](#footnote-ref-169)
169. One FTE corresponds to one employee who commits to 200 workdays of 8 hours at EUR 27.70 an hour on average. [↑](#footnote-ref-170)
170. Based on: <https://ec.europa.eu/eurostat/statistics-explained/index.php/Wages_and_labour_costs>. [↑](#footnote-ref-171)
171. For option 1a, the following labour costs would apply for the example of covering the C13 manufacture of textile subsector: EUR 136 000 recurrent labour cost. [↑](#footnote-ref-172)
172. For option 1a, the following total OOPC is estimated for the example of covering the C13 manufacture of textile subsector: EUR 11 200 recurrent expenses. [↑](#footnote-ref-173)
173. [McKinsey Global Institute, 2017](javascript:;). [↑](#footnote-ref-174)
174. E.g. Dodd-Frank Act, Modern Slavery Act, Duty of Vigilance Law, Conflict Minerals regulation, etc. [↑](#footnote-ref-175)
175. Recent available evidence shows positive impacts, e.g. [Evaluation de la mise en œuvre de la loi relative au devoir de vigilance](https://www.economie.gouv.fr/files/files/directions_services/cge/devoirs-vigilances-entreprises.pdf), January 2020 [↑](#footnote-ref-176)
176. A [study on the UK Modern Slavery Act](https://www.ethicaltrade.org/sites/default/files/shared_resources/corporate_leadership_on_modern_slavery_full_report_2016.pdf) shows that the Act has been instrumental in raising awareness of modern slavery in all supply chain tiers. Through training and awareness campaigns, senior business leaders have been made aware of the issues in their operations and have been able to effectively launch culture change and response efforts within their organisations. [↑](#footnote-ref-177)
177. E.g. In addition to [Open public consultation on sustainable corporate governance](https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12548-Sustainable-corporate-governance/public-consultation_en) evidence pointing to the benefit of increased up take of value–chain due diligence, the [Study on due diligence requirements through the supply chain](https://op.europa.eu/nl/publication-detail/-/publication/8ba0a8fd-4c83-11ea-b8b7-01aa75ed71a1/language-en) (2020) pg. 468 and 510. found that requirements from EU companies could make it easier for the host countries of the supply chain companies to implement labour standards in practice and thus support creating a level-playing in the host country of the supply chain company, therefore yielding a positive effect on the workforce in third-countries and enabling the third-country companies active on the EU market and falling under the same requirements to further leverage this positive effect in their home country or region.; Zooming in on the minerals sector [UN group of experts](https://www.undocs.org/S/2020/482) (2021), pg. 21 found that due diligence programmes have improved transparency and security in the tin, tungsten and tantalum (3T) sector in the Great Lakes region.; Zooming in on the garment sector OECD (2020): [OECD Feasibility Study: Measuring the Uptake and Impact of Due Diligence in the Garment and Footwear Sector Supply Chain](http://mneguidelines.oecd.org/OECD-feasibility-study.pdf) (pp. 102-106) found links between responsible sourcing practices and addressing decent work deficits, such as improved safety conditions in those factories that are identified as part of the global supply chain under the Bangladesh Accord, and reducing the worst impacts on workers during COVID 19 as evidenced by ACT (2020) [From COVID-19 to Living Wages](https://actonlivingwages.com/app/uploads/2021/04/From-COVID-19-to-Living-Wages-ACT-Report-2.pdf). [↑](#footnote-ref-178)
178. E.g. Rauter (2020) [The Effect of Mandatory Extraction Payment Disclosures on Corporate Payment and Investment Policies Abroad](https://onlinelibrary.wiley.com/doi/10.1111/1475-679X.12332), provides evidence that detailed disclosures about extraction payments to foreign host governments, per Dodd-Frank Act Section 1504, reduce illicit payment practices.; Schütte (2019) [International mineral trade on the background of due diligence regulation: A case study of tantalum and tin supply chains from East and Central Africa](https://www.sciencedirect.com/science/article/pii/S0301420718304720?dgcid=rss_sd_all) finds evidence for one of the mechanisms by which due diligence brings about positive impacts: “Mineral origin declarations show progressively increasing geological and logistical plausibility likely reflecting a reduction of intra-regional smuggling and more accurate chain of custody documentation. As such, international mineral trade data become more consistent with on-going implementation of due diligence.” [↑](#footnote-ref-179)
179. EU’s impact assessment on the EU Conflict Minerals Regulations, Available at: <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52014SC0053&from=EN> [↑](#footnote-ref-180)
180. E.g. PRG, IPIS, SFR, and Ulula (2020): [Evaluating Due Diligence Programs for Conflict Minerals: A Matched Analysis of 3T Mines in Eastern DRC](https://ipisresearch.be/wp-content/uploads/2021/03/eval-ddp-20210217.pdf) found that in areas where due diligence programmes exist, military interference in mining decreased, and public services and revenue increased. (p. 3 [27% less armed forces presence and 58% more tax collection and service provision]); Berkely, Seoul, Illinois (2021) [The Real Effects of Conflict Minerals Disclosures](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3908233) found that conflicts in covered-countries’ mining regions decrease by roughly 15%, on average, after the conflict minerals disclosure mandate and conflicts did not spillover to other regions within the nation. [↑](#footnote-ref-181)
181. DAI Sustainable Business Group: DAI Supplementary Analysis to the Impact Assessment on the European Commission’s Sustainable Corporate Governance Initiative, 12 March 2021; E.g. Developing countries themselves are in the process of reviewing or passing new legislation. [In 2019 Kenya](https://globalnaps.org/wp-content/uploads/2021/03/Kenya-NAP-Case-study.pdf) become the first African country to develop a National Action Plan on Business and Human Rights (NAP). Other African countries such as [Zambia, Uganda, Liberia and Morocco](https://www.business-humanrights.org/en/blog/is-it-time-for-african-countries-to-introduce-mandatory-due-diligence-on-human-rights/https:/www.business-humanrights.org/en/blog/is-it-time-for-african-countries-to-introduce-mandatory-due-diligence-on-human-rights/) are also developing their own NAPs. Labour rights and working conditions are already regulated at both national and international level but enforcement is problematic. Insofar as mandatory due diligence would add a legally binding dimension to these existing expectations, it is likely to increase the practical uptake of those existing standards, thereby improving the labour conditions in question. [↑](#footnote-ref-182)
182. E.g. In high- risk areas, through the due diligence process foreign companies undertake more efforts to obtain their “social license to operate”. [↑](#footnote-ref-183)
183. OECD (2016) [Do environmental policies affect global value chains?](https://www.oecd-ilibrary.org/economics/do-environmental-policies-affect-global-value-chains_5jm2hh7nf3wd-en;jsessionid=3OnZN9jRk9Mep-C0iuEDISdB.ip-10-240-5-162), and OECD (2018) [Green policies and firms’ competitiveness](https://www.oecd.org/greengrowth/GGSD_2018_Competitiveness%20Issue%20Paper_WEB.pdf); exemplify how regulation can have a positive effect on global value chain integration, competitiveness, productivity, innovation, etc. E.g. As evidenced by DAI Sustainable Business Group, project procurement experts in Nigeria report that the simple act of a multinational asking due diligence questions as part of their local procurement process prompts local businesses to put measures in place so that they can improve their standards, be more responsible and become more attractive and competitive business partners. [↑](#footnote-ref-184)
184. E.g. Christensen et al. (2017) [The real effects of mandated information on social responsibility in financial reports: Evidence from mine-safety records](https://clear.dol.gov/Study/real-effects-mandated-information-social-responsibility-financial-reports-Evidence-mine), shows that when mine owners are obligated to disclose safety performance information in their 10-K filings, per Dodd-Frank Act Section 1503, they are incentivized to increase investments in that domain. [↑](#footnote-ref-185)
185. For further details prefer refer to economic impacts. [↑](#footnote-ref-186)
186. Women, indigenous people, elderly persons, persons with disabilities, children as well as religious or ethical minorities are considered groups that are likely to face higher risks regarding potentially harmful practices and impacts. [↑](#footnote-ref-187)
187. [UN Global Compact Bulletin](https://www.unglobalcompact.org/library/3051) (2015). E.g. Mésonnier, Nguyen (2021) [Showing off cleaner hands: mandatory climate-related disclosure by financial institutions and the financing of fossil energy](https://publications.banque-france.fr/sites/default/files/medias/documents/wp800.pdf) shows how already mandatory climate disclosure regulations introduced in France have contributed to French investors curbing their investments in fossil fuel companies by 40%. [↑](#footnote-ref-188)
188. DAI Sustainable Business Group: DAI Supplementary Analysis to the Impact Assessment on the European Commission’s Sustainable Corporate Governance Initiative, 12 March 2021 [↑](#footnote-ref-189)
189. E.g. In addition to providing for ambitious trade and sustainable development chapters, the sustainability dimension will continue to be reflected in many other aspects of the EU’s trade and investment agreements, as foreseen by the [Trade Policy Review](https://trade.ec.europa.eu/doclib/docs/2021/february/tradoc_159438.pdf) (2021), p. 12. [↑](#footnote-ref-190)
190. Impacts for rights-holders could result in unintended consequences when mandatory due diligence obligations are imposed only for certain geographical regions, as this allows businesses to move to other areas of supply where these due diligence requirements do not apply, causing a demand drop and bringing about negative impacts, e.g. relating to the right to food, the right to education, and the right to health in the case of the Dodd-Frank Act, as evidenced by a study by the University of Texas School Of Law (Owen M., 2013). This is less likely to apply if the due diligence requirements were imposed on a wider group of businesses operating globally, as evidenced by the [Study on due diligence requirements through the supply chain](https://op.europa.eu/en/publication-detail/-/publication/8ba0a8fd-4c83-11ea-b8b7-01aa75ed71a1/language-en) (2020), p.525. [↑](#footnote-ref-191)
191. Respondents to the [Commission open public consultation on the sustainable corporate governance initiative](https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12548-Sustainable-corporate-governance/public-consultation_en) (2021) as well as [Study on due diligence requirements through the supply chain](https://op.europa.eu/nl/publication-detail/-/publication/8ba0a8fd-4c83-11ea-b8b7-01aa75ed71a1/language-en) (2020) pg.16, indicate that divestment is the least preferred due diligence action. [↑](#footnote-ref-192)
192. This is counterproductive regarding the social inclusion goals. [↑](#footnote-ref-193)
193. According to the findings of the [Study on due diligence requirements through the supply chain](https://op.europa.eu/en/publication-detail/-/publication/8ba0a8fd-4c83-11ea-b8b7-01aa75ed71a1/language-en) (p.526), the extent of this possibility is context-specific as a stronger regulatory environment may have regional effects and either pressurize governments in a host or third country to adopt similar legislation or hold companies in a host or third country accountable to follow suit voluntarily. [↑](#footnote-ref-194)
194. DAI Sustainable Business Group: DAI Supplementary Analysis to the Impact Assessment on the European Commission’s Sustainable Corporate Governance Initiative, 12 March 2021. [↑](#footnote-ref-195)
195. E.g. Business and HR Resource Centre (2019) [Fast & Fair Renewable Energy Investments,](https://old.business-humanrights.org/sites/default/files/Renewable%20Energy%20Investor%20Briefing_0.pdf) list successful examples of stakeholder engagement as part of due diligence from countries across the globe, as follows: Canadian W Dusk Group empowers communities through indigenous ownership of renewable energy by consulting with councils of elder community leaders on projects and the community shares the benefits from the electricity produced; USAs Solar Holle creates sustainable jobs through a just transition by training solar installers in West Virginia in the United States, a region known for the dominance of coal mining in its economy, thereby mitigating the social and economic hardships the region’s residents face with shrinking jobs in the coal sector; New Zelands Contact Energy established mutually beneficial relationships with Maori land trust leaders, who own land that includes vast geothermal steam fields, through extensive consultation outlining benefit-sharing and monitoring of respect for communities’ rights.; Chiles Enel Generación withdrew its water rights in response to community concerns and the lack of free, prior, and informed consent regardless of already having invested considerably in the project. [↑](#footnote-ref-196)
196. By lowering the risk of doing business with local suppliers in developing countries, this support is also immediately benefitting EU companies. [↑](#footnote-ref-197)
197. Meaningful engagement with stakeholders is attainable as can be seen for examples such as shown in Business and HR Resource Centre (2021) [All at sea: An evaluation of company efforts to address modern slavery in pacific supply chains of canned tuna](https://media.business-humanrights.org/media/documents/Tuna_II_v6.pdf), where Thai Union’s “Tell Us” project aims to strengthen worker voice mechanisms by implementing a standard operating procedure for handling workers’ voice, internal key performance indicators on worker voice management and guidelines for providing remediation to workers or the Rio Tinto’s ‘New Country Entry’ process in collaboration with the Danish Institute for Human Rights (DIHR) which identified major risk and needs for engagement with indigenous peoples an implemented proactive mitigation strategies. [↑](#footnote-ref-198)
198. McKinsey (2017) Sustainability’s deepening imprint. Available at: [https://www.mckinsey.com/business-functions/sustainability/our-insights/sustainabilitys-deepening-imprint#](https://www.mckinsey.com/business-functions/sustainability/our-insights/sustainabilitys-deepening-imprint). [↑](#footnote-ref-199)
199. Clark, Gordon L. and Feiner, Andreas and Viehs, Michael (2015). From the Stockholder to the Stakeholder: How Sustainability Can Drive Financial Outperformance. Available at SSRN: https://ssrn.com/abstract=2508281 or http://dx.doi.org/10.2139/ssrn.2508281 NOTE 40. [↑](#footnote-ref-200)
200. Edmans, A. (2012). T[he Link Between Job Satisfaction and Firm Value, with Implications for Corporate Social Responsibility](https://ssrn.com/abstract=2054066%20or%20http:/dx.doi.org/10.2139/ssrn.2054066). Academy of Management Perspectives 26(4), 1-19, November 2012. Available at SSRN: https://ssrn.com/abstract=2054066 or <http://dx.doi.org/10.2139/ssrn.2054066>. [↑](#footnote-ref-201)
201. German Watch: Sydow J. & Reichwein A., 2018. [↑](#footnote-ref-202)
202. Additionally, a few indirect advances for rights-holders were found around improved safety and health standards for miners, and the implementation of a regional certification system for mines as conflict-free. When 193 mines were assessed under this certification scheme in Eastern Congo to investigate conflict and child labour, 166 of the mines (86%) successfully passed the assessment. [↑](#footnote-ref-203)
203. The Boliden case is a good example of this. In the 1980s, Boliden paid Promel to export industrial waste to Chile, where Promel disposed of it without removing the arsenic. This caused awful health effects, including cancers and neurological disorders, for people living near the site. In 2013 victims took legal action against Boliden in the Swedish courts arguing that Boliden had breached a duty to ensure that the sludge was appropriately processed by Promel, but eventually lost their case. In March 2019, after the claimants appealed, the court decided to apply Swedish law and dismissed the appeal on the basis: that the claim for damages had been filed too late and the cause of action was time-barred. Boliden has not faced legal consequences for this negligence. The KiK case led to a similar outcome. On 11 September 2012, 258 workers died and hundreds were seriously injured when a fire broke out in the Ali Enterprise garment factory in Karachi, Pakistan. Due to lax fire safety measures, workers were at first unaware of and then trapped by the fire. At the time, the factory was producing jeans for its main client, German retailer KiK. Victims sought justice in the German courts, but the court decided to apply Pakistani law, as this was where the harm occurred, and dismissed the action, deciding that according to Pakistani law the statute of limitation had expired and the claimants were too late to seek justice. The Shell case is further proof of said obstacles. Shell is ravaging the Niger Delta through its decades-long quest for oil. Pollution caused by the activities of its subsidiary SPDC is having a devastating effect on both the ecosystem and people living in this area. Victims sued the company before Dutch courts, but claimants have faced legal barriers, challenges and uncertainty. [↑](#footnote-ref-204)
204. DAI Supplementary Analysis to the Impact Assessment on the European Commission’s Sustainable Corporate Governance Initiative, 2021 [↑](#footnote-ref-205)
205. Commission Staff Working Document Accompanying document to the Proposal for a Directive of the European Parliament and of the Council on the protection of the environment through criminal law. [IMPACT ASSESSMENT](https://ec.europa.eu/smart-regulation/impact/ia_carried_out/docs/ia_2007/sec_2007_0160_en.pdf). [↑](#footnote-ref-206)
206. Same as above. [↑](#footnote-ref-207)
207. Supporting study on due diligence. [↑](#footnote-ref-208)
208. The most listed existing standards that should be taken into account, according to respondents, are Paris agreement, EU 2050 long-term strategy (objective of climate neutrality, objective of zero net loss of biodiversity), Convention on Biological Diversity, Aichi Biodiversity Targets, EU Biodiversity strategy for 2030, EU textile strategy, Sustainable Product initiative, Thresholds in the Post 2021 Global Biodiversity Framework, REACH (Registration, Evaluation, Authorisation and Restriction of Chemicals), EU Plastic Strategy and Circular Economy action plan, New EU legislation on deforestation under consideration. [↑](#footnote-ref-209)
209. This ratio also depends on the definition of midcaps that would be excluded from the full due diligence obligation in the preferred options, similarly to medium-sized companies (in high-impact sectors). [↑](#footnote-ref-210)
210. Supporting study on due diligence [↑](#footnote-ref-211)
211. Interim report of EC study “Uptake of CSR by SMEs and start-ups in Europe”. [↑](#footnote-ref-212)
212. The Dutch evaluation of its national Responsible Business Conduct agreements finds that SMEs are more likely to have little or no prior experience with due diligence, to experience internal capacity and financial constraints to implement it, have limited leverage –especially beyond the first tier and with bigger suppliers-. It raises concerns that companies do not establish adequate individual complaints mechanisms and smaller companies, in particular, may lack the required resources and capacities. It brings the example of the gold agreement, where medium and large companies are expected to sign the agreement, while smaller operators sign a separate code of conduct, which is in line with OECD Guidelines and designed particularly to take account of their size (in line with the proportionality provision in the UNGPs, which states that “the means through which a business enterprise meets its responsibility to respect human rights will be proportional to, among other factors, its size” (UN, 2011)). In practice, companies commit to checking whether their gold suppliers are a member of the RBC agreement and/or have due diligence in place and to report their findings to their association secretariat.

     Similarly, the Timber regulation 2016 evaluation showed that compliance is difficult for small and micros, which are in a disadvantaged position due to their low economies of scale (as the costs of the DDS need to be covered by a lower turnover), and that, while the economic consequences of the EUTR may be bearable for large and some medium-sized firms, many small and micro firms had not only not implemented the Regulation and were still unaware of its implications. [↑](#footnote-ref-213)
213. See Supporting study on due diligence, p. 445, also referring to other relevant studies. [↑](#footnote-ref-214)
214. <https://opentrustfabric.org/otf-at-endorse-event-2/>. [↑](#footnote-ref-215)
215. <https://www.copernicus.eu/en>. [↑](#footnote-ref-216)
216. <https://www.airbus.com/newsroom/stories/starling.html>. [↑](#footnote-ref-217)
217. There are also multi-stakeholder instruments, like the Dutch "https://www.imvoconvenanten.nl/en/metals-sector/convenant" International Responsible Business Conduct Agreement for the Metals Sector prepared to identify, prevent and address risks to people and the environment across the entire wind industry’s value chain, from risks related the extraction of raw materials through the decommissioning of wind farms. [↑](#footnote-ref-218)
218. Blome, C. 2016. [Stopping Conflict Minerals with OECD Guidance for Mineral Supply Chain](http://sro.sussex.ac.uk/id/eprint/65452/1/__smbhome.uscs.susx.ac.uk_tjk30_Documents_BlomeHofmannSchleper%20-%20Stopping%20conflict%20minerals%20with%20the%20OECD%20guidance%20for%20responsible%20mineral%20supply%20chains.pdf), University of Sussex, School of Business, Management and Economics (Table 2). [↑](#footnote-ref-219)
219. [Evaluation of the Dutch Responsible Business Conduct Agreements - KIT Royal Tropical Institute](https://www.kit.nl/evaluation-of-the-dutch-responsible-business-conduct-agreements/) [↑](#footnote-ref-220)
220. For instance, cement production will help recycle wind turbine blades, PET bottles are used by the textile industry. The chemical industry plays an important role in the transition to a circular economy by investing in the research and development of new materials but innovation is also facilitated by the collaboration of the sectors affected. [↑](#footnote-ref-221)
221. [AD\_Enquête\_BPI\_France\_ORSE\_2019 (novethic.fr)](https://www.novethic.fr/fileadmin/user_upload/tx_ausynovethicarticles/BH/AD_Enqu%C3%AAte_BPI_France_ORSE_2019_Web.pdf), [Devoir de vigilance : les PME en première ligne, sans être assez accompagnées par les donneurs d'ordre (novethic.fr)](https://www.novethic.fr/actualite/entreprise-responsable/isr-rse/rse-et-devoir-de-vigilance-les-pme-en-premiere-ligne-sans-avoir-toujours-les-moyens-adequats-148094.html) [↑](#footnote-ref-222)
222. First of all, the costs are based on a survey that inquired companies about the (directly incurred) cost of due diligence activities covering the entire supply chains. Secondly, the estimates of large companies were used as a basis and as such, extrapolating to SMEs (and especially to small companies) that are only active in sectors where the risks of adverse impacts is not high should be done in a careful way. [↑](#footnote-ref-223)
223. See Shareholder Rights Directive II. [↑](#footnote-ref-224)
224. Existing across all Member States. The Accounting Directive (Directive 2013/34/EU) promoted the application of such codes on a “comply or explain” basis, i.e. listed companies are required to refer in their corporate governance statement to a code and disclose whether they comply with it and if not, they provide an explanation (see Article 20). [↑](#footnote-ref-225)
225. Commission Recommendations 2004/913/EC, 2005/162/EC and 2009/385/EC. [↑](#footnote-ref-226)
226. Report on the application of the Commission Recommendation on directors’ remuneration (SEC 2007, 1022), Report on the application of the Commission 2009/385/EC Recommendation (SEC(2010)285). [↑](#footnote-ref-227)
227. Directive 2013/36/EU on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC (CRD IV), as amended, among others, by Directive (EU) 2019/878 as regards exempted entities, financial holding companies, mixed financial holding companies, remuneration, supervisory measures and powers and capital conservation measures (CRD V). [↑](#footnote-ref-228)
228. Article 449a of Regulation (EU) No 575/2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (CRR), as amended by Regulation (EU) 2019/876 as regards the leverage ratio, the net stable funding ratio, requirements for own funds and eligible liabilities, counterparty credit risk, market risk, exposures to central counterparties, exposures to collective investment undertakings, large exposures, reporting and disclosure requirements. [↑](#footnote-ref-229)
229. E.g. the CRD imposes a ratio between the variable and the fixed component of remuneration. [↑](#footnote-ref-230)
230. Directive 2014/95/EU, amending the Accounting Directive (Directive 2013/34/EU), now under revision. [↑](#footnote-ref-231)
231. Sustainability reporting obligation for all large companies as defined by the Directive and, as of 2026, to companies (including non-EU companies, excluding all micro enterprises) listed on EU regulated markets. [↑](#footnote-ref-232)
232. Regulation (EU) 2019/2088 on sustainability‐related disclosures in the financial services sector. Financial market participants have to comply with the SFDR as from 10 March 2021. [↑](#footnote-ref-233)
233. Regulation (EU) 2020/852 on the establishment of a framework to facilitate sustainable investment, and amending Regulation (EU) 2019/2088. [↑](#footnote-ref-234)
234. [↑](#footnote-ref-235)
235. Directive 2004/109/EC, amended by Directive 2013/50/EU. [↑](#footnote-ref-236)
236. Directive 2004/25/EC, amended by Regulation (EC) 219/2009 and Directive 2014/59/EU. [↑](#footnote-ref-237)
237. In addition, the Posting of Workers Enforcement Directive (Directive 2014/67/EU) gives Member States the option to provide that a subcontractor should not be liable in specific circumstances or that the liability may be limited in cases where that subcontractor has undertaken due diligence obligations. [↑](#footnote-ref-238)
238. Loi n° 2017-399 du 27 mars 2017 relative au devoir de vigilance des sociétés mères et des entreprises donneuses d'ordre. [↑](#footnote-ref-239)
239. <https://zoek.officielebekendmakingen.nl/stb-2019-401.html>. [↑](#footnote-ref-240)
240. <https://www.parlament.gv.at/PAKT/VHG/XXVII/A/A_00579/index.shtml>. [↑](#footnote-ref-241)
241. See <https://www.ft.dk/samling/20181/beslutningsforslag/b82/20181_b82_som_fremsat.htm>. [↑](#footnote-ref-242)
242. <https://www.tweedekamer.nl/kamerstukken/wetsvoorstellen/detail?id=2021Z04465&dossier=35761>. [↑](#footnote-ref-243)
243. See <https://www.business-humanrights.org/en/latest-news/national-regional-movements-for-mandatory-human-rights-environmental-due-diligence-in-europe/>. [↑](#footnote-ref-244)
244. Plan d’Action pour la Croissance et la Transformation des Entreprises, also known as the [Loi PACTE](https://www.economie.gouv.fr/plan-entreprises-pacte), the “PACTE Law”, enacted in May 2019. [↑](#footnote-ref-245)
245. According to its principle 2.2, “in order to pursue sustainable value creation, the board prepares an inclusive approach, equilibrating the interests and legitimate expectations of the shareholders and the other stakeholders”

     (<https://www.corporategovernancecommittee.be/sites/default/files/generated/files/page/code_belge_de_gouvernance_dentreprise_2020_0.pdf>). [↑](#footnote-ref-246)
246. Principle 2.4 states that “The management board and the supervisory board should ensure that decisions are made in a balanced and effective manner whilst taking account of the interests of stakeholders” (<https://www.mccg.nl/?page=4738>). [↑](#footnote-ref-247)
247. In its foreword it refers that “The Code highlights the obligation of Management Boards and Supervisory Boards – in line with the principles of the social market economy – to take into account the interests of the shareholders, the enterprise’s workforce and the other groups related to the enterprise (stakeholders) to ensure the continued existence of the enterprise and its sustainable value creation (the enterprise’s best interests).”

     (<https://www.dcgk.de//files/dcgk/usercontent/en/download/code/191216_German_Corporate_Governance_Code.pdf>). [↑](#footnote-ref-248)
248. Its article 1, principle IV mentions that “the board has to create long-term value for the benefit of shareholders, taking into account the interests of other stakeholders relevant to the company” (see <https://ecgi.global/node/8009>). [↑](#footnote-ref-249)
249. Its recommendation 12 says that “… in pursuing the company’s interest (*interés social*), apart from respecting the law and regulations and behaving in good faith, ethics and respect for the covenants and commonly accepted good practices, the board of directors should try to conciliate the company’s interest, where appropriate, with the legitimate interests of its employees, suppliers, clients and the rest of groups of stakeholders that could be affected, as well as the impact of its activities in the community as a whole and the environment.”

     (<https://www.cnmv.es/DocPortal/Publicaciones/CodigoGov/CBG_2020.pdf>). [↑](#footnote-ref-250)
250. Data on limited liability companies are taken from the 2020 CEPS’ Study on the Non-Financial Reporting Directive [reference to be updated after study published] and relate to 2016. The 13.7 million approximates the total number of companies that fall under the general scope of the Accounting Directive (Directive 2013/34/EU), including companies with otherwise unlimited liability in case all of their members have limited liability themselves. The scope includes companies taking one of the legal forms specified in the annexes of the Directive. The list of limited liability company forms is largely the same as in the Codified Company Law Directive (Directive (EU) 2017/1132 relating to certain aspects of company law), with slight differences for a few countries (incl. regarding the exclusion or inclusion of certain partnerships).

     Note that the approximation of the number of limited liability companies by CEPS is substantially higher than the number of limited liability companies in the business economy (excluding activities of holding companies) appearing in Eurostat statistics, which amounted to 8.6 million. One of the several reasons is that Eurostat structural business statistics do not count any partnerships as limited liability companies, even if they are classified as such under the Accounting Directive. [↑](#footnote-ref-251)
251. The undertaking size categories under the Accounting Directive are defined not only on the basis of the number of employees but also taking the balance sheet total and the net turnover into account. [↑](#footnote-ref-252)
252. See CEPS Study. [↑](#footnote-ref-253)
253. As regards the distribution of enterprises active in the EU-27’s non-financial business economy across economic sectors, slightly more than three quarters of them were active in the services sector, roughly 15% was in construction, and less than 10% operated in industry. (The share of the services, construction and industry sectors show the EU-28 average for 2017 [update expected for Jan 2021]: the UK had slightly larger services and smaller industry sectors.) [↑](#footnote-ref-254)
254. This is an estimate of the CEPS study that uses the definition of the Accounting Directive for both the size category and the LLCs. For the cost calculations we rely on the Orbis database which uses its own classification of LLC and which may have some data gaps (even though this is less likely in the larger size category), also using a different definitions of the size. [↑](#footnote-ref-255)
255. The share of large companies in the turnover excl. subsidiaries is slightly lower (about 75% instead of 77%) and the shares of micro and small companies respectively are slightly higher than their shares in total non-corrected turnover. This reflects the fact that there are relatively fewer subsidiaries among the micro and small companies. [↑](#footnote-ref-256)
256. Data on listed limited liability companies are also taken from the CEPS study on NFRD. [↑](#footnote-ref-257)
257. In addition, there are about 300 non-EU companies listed in the EU (about three quarters of them are domiciled in the UK), with a total turnover almost reaching EUR 1 trillion. According to the CSRD proposal, these companies would also be subject to the sustainability reporting rules. [↑](#footnote-ref-258)
258. [Final Report of the Financial Stability Board’s Task Force on Climate-related Financial Disclosure](https://assets.bbhub.io/company/sites/60/2020/10/FINAL-2017-TCFD-Report-11052018.pdf), [↑](#footnote-ref-259)
259. [TEG Final Report on Climate Benchmarks and Benchmarks’ ESG Disclosures](https://ec.europa.eu/info/sites/info/files/business_economy_euro/banking_and_finance/documents/190930-sustainable-finance-teg-final-report-climate-benchmarks-and-disclosures_en.pdf), September 2019 [↑](#footnote-ref-260)
260. Banque de France-ACPR (2017), [Evaluation des risques liés au changement climatique pour le secteur bancaire: vers des outils de stress test?](https://acpr.banque-france.fr/sites/default/files/medias/documents/20170314-climat.pdf) [↑](#footnote-ref-261)
261. Vermeulen R., Schets E., Lohuis M, Kölbl B., Jansen D.-J., and Heeringa W., (DNB, 2018), “[An energy transition risk stress test for the financial system of the Netherlands](https://www.dnb.nl/media/pdnpdalc/201810_nr-_7_-2018-_an_energy_transition_risk_stress_test_for_the_financial_system_of_the_netherlands.pdf)”. [↑](#footnote-ref-262)
262. “[Investing in a time of climate change](https://www.ifc.org/wps/wcm/connect/e9bfa328-e091-465b-9da6-8fe312261b98/Investing+in+a+time+of+climate+change.pdf?MOD=AJPERES&CVID=kTFEATf)”, Mercer 2015. [↑](#footnote-ref-263)
263. Moody’s environmental global risks heat map updated in September 2018: it finds that 11 sectors with $2.2 trillion debt have elevated climate risk exposure: Coal mining, Coal terminals, Utilities and power companies, Power generation projects, Oil and gas exploration and production, Oil and gas refining and marketing, Metal and mineral mining (excluding coal), Commodity chemicals, Building materials (incl. cement), Steel, Automotive manufacturers. Moody’s finds that an additional 22 sectors with $10.1 trillion in rated debt (13.5% of the total) face moderate environmental risks. Finally, 51 sectors with $62.3 trillion in rated debt (83.5% of the total) have low exposure to environmental risks. The report, which is an update to the initial 2015 study, assesses the exposure of 84 industry sectors covering $74.6 trillion of debt. [↑](#footnote-ref-264)
264. ECB, [Guide on climate-related and environmental risks](https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.202011finalguideonclimate-relatedandenvironmentalrisks~58213f6564.en.pdf). [↑](#footnote-ref-265)
265. see footnote 154 [↑](#footnote-ref-266)
266. <https://ec.europa.eu/clima/policies/adaptation/how/sectors_en> [↑](#footnote-ref-267)
267. See the 2019 OECD report on business and biodiversity and OECD publication on [Biodiversity, natural capital and the economy](https://www.oecd.org/environment/biodiversity-natural-capital-and-the-economy-1a1ae114-en.htm) (May 2021). [↑](#footnote-ref-268)
268. World Economic Forum, [The Global Risk Report 2021](http://www3.weforum.org/docs/WEF_The_Global_Risks_Report_2021.pdf). [↑](#footnote-ref-269)
269. See also World Economic Form [The Future Of Nature And Business](http://www3.weforum.org/docs/WEF_The_Future_Of_Nature_And_Business_2020.pdf) (2020). [↑](#footnote-ref-270)
270. McKinsey, 2020 (Woetzel J., Pinner D., Samandari H., Engel H., Krishnan M., Kampel C., and Graabak J.): [Could climate become the weak link in your supply chain?](https://www.mckinsey.com/business-functions/sustainability/our-insights/could-climate-become-the-weak-link-in-your-supply-chain). [↑](#footnote-ref-271)
271. WWF (2019), [Hidden Risks and Untapped Opportunities: Water and the Indian Banking Sector](https://wwf.panda.org/our_work/finance/?341851/Increasing-water-risks-threaten-to-strand-substantial-assets-of-Indian-banks). [↑](#footnote-ref-272)
272. <https://www.theguardian.com/sustainable-business/dyeing-textile-sector-water-risks-adidas>, European Parliamentary Research Service (2019), [Environmental impact of the textile and clothing industry](https://www.europarl.europa.eu/RegData/etudes/BRIE/2019/633143/EPRS_BRI(2019)633143_EN.pdf). [↑](#footnote-ref-273)
273. Kiel Institute for the World Economy, [Kiel Working Paper No. 2155](https://www.ifw-kiel.de/fileadmin/Dateiverwaltung/IfW-Publications/Saskia_Moesle/KWP_2155_low_water_econ_activity.pdf), (April 2020). [↑](#footnote-ref-274)
274. Indeed, the company suffered not only financially, but also from a reputational and legal perspective. The total costs to BP are hard to estimate with accuracy. The Economist estimated USD 42 billion in clean-up and compensation costs, whereas the Financial Times estimated that the clean-up costs alone may have amounted to USD 90 billion. According to the International Finance Corporation (see: [The Business Case for Sustainability](https://www.cbd.int/financial/mainstream/ifc-businesscase.pdf)), BP lost more than $32 million a day in brand value after the oil spill, and BP’s market value dropped from USD 184 billion to 96.5 billion, roughly 48 percent in a period of two months. [↑](#footnote-ref-275)
275. BIICL and LSE study on due diligence requirements through the supply chain, 2020 [↑](#footnote-ref-276)
276. Wilson J., Consumer preferences continue to shift towards sustainability, market research shows. TriplePundit, November 2018 (<https://www.triplepundit.com/story/2018/consumer-preferences-continue-shift-toward-sustainability-market-research-shows/55496>). [↑](#footnote-ref-277)
277. The Bank of England shows that global economic losses from extreme weather events have been constantly increasing, see [Climate change: why it matters to the Bank of England?](https://www.bankofengland.co.uk/knowledgebank/climate-change-why-it-matters-to-the-bank-of-england) and [Climate change: what are the risks to financial stability?](https://www.bankofengland.co.uk/knowledgebank/climate-change-why-it-matters-to-the-bank-of-england) . See also [Shining a light on climate risks: the ECB’s economy-wide climate stress test](https://www.ecb.europa.eu/press/blog/date/2021/html/ecb.blog210318~3bbc68ffc5.en.html) (2021). [↑](#footnote-ref-278)
278. See [The Global Risk Report 2021](http://www3.weforum.org/docs/WEF_The_Global_Risks_Report_2021.pdf) referred to above. [↑](#footnote-ref-279)
279. The IPCC [Special Report 2018](https://www.ipcc.ch/sr15/download/) finds that every year’s delay before initiating emission reductions decreases the available time to reach zero emissions on a pathway remaining below 1.5°C by approximately two years. The World Meteorological Organization’s [Global Annual to Decadal Climate Update](https://hadleyserver.metoffice.gov.uk/wmolc/WMO_GADCU_2020.pdf) forecasts increased temperatures until 2025 in almost all regions of the world, with more rain or tropical cyclones in certain regions. This increases physical risks to companies related to climate change. [↑](#footnote-ref-280)
280. Wilson J., [Consumer preferences continue to shift towards sustainability, market research shows.](https://www.triplepundit.com/story/2018/consumer-preferences-continue-shift-toward-sustainability-market-research-shows/55496) TriplePundit, November 2018. See also the [study on EU market for sustainable products, the retail perspective on sourcing policies and consumer demand](https://www.intracen.org/uploadedFiles/intracenorg/Content/Publications/EU%20Market%20for%20Sustainable%20Products_Report_final_low_res.pdf). [↑](#footnote-ref-281)
281. See Institutional Investors Group on Climate Change [Investor Expectations for Paris-aligned Accounts](https://urldefense.com/v3/__https:/www.iigcc.org/download/investor-expectations-for-paris-aligned-accounts/?wpdmdl=4001&refresh=60953935763d21620392245__;!!DOxrgLBm!S21Ms7d1GMGDce_Hbin-hcr42AFpllZi-MZNZBxYPsygJV8Ta7dEnkG9uTJhmUiu02SmZLhb$) (2020). [↑](#footnote-ref-282)
282. See Commission SWD “[Closing the climate protection gap - scoping policy and data gaps”,](https://ec.europa.eu/clima/sites/default/files/adaptation/what/docs/swd_2021_123_en.pdf) May 2021 [↑](#footnote-ref-283)
283. 2020 [TCFD status report](https://assets.bbhub.io/company/sites/60/2020/09/2020-TCFD_Status-Report.pdf) on about 1,700 public companies for the 2017-2019 period [↑](#footnote-ref-284)
284. Referred to above. [↑](#footnote-ref-285)
285. See the report on [SMEs and the Environment in the European Union](https://op.europa.eu/en/publication-detail/-/publication/aa507ab8-1a2a-4bf1-86de-5a60d14a3977) (Calogirou et al. 2010). [↑](#footnote-ref-286)
286. [2019 Research Report of the Alliance for Corporate Transparency](https://en.frankbold.org/sites/default/files/publikace/analyza_1000_korporaci.pdf). [↑](#footnote-ref-287)
287. [“Xinjiang cotton sparks concern over 'forced labour' claims](https://www.bbc.com/news/business-50312010)”. BBC, 13 November 2019 [↑](#footnote-ref-288)
288. <https://www.economist.com/business/2021/03/27/china-boycotts-western-clothes-brands-over-xinjiang-cotton> [↑](#footnote-ref-289)
289. ECCJ’s “[What if? Case studies of human rights abuses and environmental harm linked to EU companies, and how EU due diligence laws could help protect people and the planet](https://corporatejustice.org/asi_eccj_report_final.pdf)” [↑](#footnote-ref-290)
290. In North and South America, in Afghanistan, in Myanmar, and in West Africa, and extends beyond 3TG, including iron, jade, and talc. [↑](#footnote-ref-291)
291. Child labour is reported to be occurring in coal in Colombia, zinc in Bolivia, and diamonds in Angola and Central African Republic, but the overwhelming amount of attention is currently given to child labour in cobalt mining from the DRC. OECD (2021): [Trends in Stakeholder Reporting: Mineral Supply Chains (oecd.org)](http://mneguidelines.oecd.org/trends-in-stakeholder-reporting-mineral-supply-chains.pdf), see p. 32 illustrating how frequently EU companies are involved in supply chains where serious abuses of human rights are reported, including any forms of torture, cruel, inhuman and degrading treatment, forced or compulsory labour, worst forms of child labour, war crimes and other violations of international humanitarian law (IHL), crimes against humanity (CAH), genocide, and other “gross” human rights abuses such as gender or sexual based violence. [↑](#footnote-ref-292)
292. Assessing Progress in Reducing Child Labor in Cocoa Growing Areas of Côte d’Ivoire and Ghana by NORC at the University of Chicago: <https://www.norc.org/Research/Projects/Pages/assessing-progress-in-reducing-child-labor-in-cocoa-growing-areas-of-c%C3%B4te-d%E2%80%99ivoire-and-ghana.aspx> . A survey conducted by NORC showed that amid a 14 percent increase in cocoa production between 2013-14 and 2018-19 in Côte d’Ivoire and Ghana in aggregate, the prevalence of child labour in cocoa production among cocoa growing households in each individual country remained stable. [↑](#footnote-ref-293)
293. EP, [Cocoa infograph](https://www.europarl.europa.eu/resources/library/media/20120314MLT40774/20120314MLT40774.pdf) – EU international trade agreement [↑](#footnote-ref-294)
294. [SDSN, Social spillover effects in the EU’s textile supply chains](https://irp-cdn.multiscreensite.com/be6d1d56/files/uploaded/Social%20Spillover%20%20Effects%20in%20the%20EU%27s%20Textile%20Supply%20Chain.pdf). October 2020. [↑](#footnote-ref-295)
295. See the ECCJ “[What if? Case studies of human rights abuses and environmental harm linked to EU companies, and how EU due diligence laws could help protect people and the planet](https://corporatejustice.org/asi_eccj_report_final.pdf)” for examples regarding the manufacturing industry, and for an example on VEON Ltd and labour rights of telecommunication employees in Bangladesh, including violation of the right to freedom of association, with workers and union representatives subject to threats, harassment or unlawful dismissals. Regarding the agricultural sector, see [Alessandra Corrado “Migrant crop pickers in Italy and Spain”, Heinrich Böll Foundation](https://www.boell.de/sites/default/files/e-paper_migrant-crop-pickers-in-italy-and-spain_1.pdf#:~:text=In%20the%20Mediterranean%20basin%2C%20Spain%20and%20Italy%20are,restructuring%20processes%20it%20has%20experienced%20since%20the%20mid-1980s.). As regards the construction sector, examples are cases of exploitation of migrant workers in Qatar, at Irish company Mercury MENA and French company Vinci’s construction sites for the 2022 football World Cup. See Amnesty International, “[Unpaid and abandoned: the abuse of Mercury MENA workers](https://www.amnesty.org/en/latest/research/2018/09/mercury-mena-abuses-qatar/)”. See BHRRC, “[Vinci lawsuits (re forced labour in Qatar)](https://www.business-humanrights.org/en/latest-news/vinci-lawsuits-re-forced-labour-in-qatar/)”. [↑](#footnote-ref-296)
296. The EU is highly dependent on resources extracted or used outside Europe. Depending on the type of resource, the associated total environmental footprint of EU consumption that occurs outside Europe is estimated to be in the range of 30-60%, whereby land use and water use account for around 60%. See <https://www.eea.europa.eu/publications/soer-2020>, p.34, 49, 50. [↑](#footnote-ref-297)
297. [The structure, drivers and policy implications of the European carbon footprint](https://www.tandfonline.com/doi/full/10.1080/14693062.2019.1639489?src=recsys) (2019). Richard Wood, Karsten Neuhoff, Dan Moran, Moana Simas, Michael Grubb & Konstantin Stadler. [↑](#footnote-ref-298)
298. [corporate-action-on-ghg-emissions-ecovadis.pdf](file:///C:\Users\kereczs\Downloads\corporate-action-on-ghg-emissions-ecovadis.pdf) [↑](#footnote-ref-299)
299. See Supporting study on due diligence, p. 215 describing the example of oil spills arising out of the activities of the Nigerian subsidiary of Anglo-Dutch company Shell in the Niger Delta, BP which was accused of causing environmental damage to the land of Colombian farmers (including cutting across key water sources which caused soil erosion and spoiled crops and fish ponds) as a result of the construction of an oil pipeline. [↑](#footnote-ref-300)
300. See Supporting study on due diligence, p. 215 describing the following examples: Dutch company Trafigura Beheer disposing toxic waste in Cote d’Ivoire affecting 100,000 residents. Swedish mining company Boliden was accused of disposing industrial waste in Chile causing cancer as adverse environmental impacts. [↑](#footnote-ref-301)
301. Commission Delegated Regulation (EU) 2020/1816 supplementing Regulation (EU) 2016/1011 as regards the explanation in the benchmark statement of how environmental, social and governance factors are reflected in each benchmark provided and published. [↑](#footnote-ref-302)
302. Calculated here for demonstration purposes using the second variant for defining midcap companies, i.e. all LLCs with more than 50 employees and more than EUR 8 million turnover would be covered, except for companies with more than 500 employees and more than EUR 150 million turnover (very large companies).

     The second number indicates the number with indirectly impacted subsidiaries excluded. [↑](#footnote-ref-303)
303. See EU Emissions Trading System Data Viewer, Background note, by the European Environment Agency, <https://www.eea.europa.eu/data-and-maps/data/european-union-emissions-trading-scheme-12/eu-ets-background-note/eu-ets-background-note/download>. [↑](#footnote-ref-304)
304. Regulation (EU) 2016/1011 of the European Parliament and of the Council of 8 June 2016 on indices used as benchmarks in financial instruments and financial contracts or to measure the performance of investment funds and amending Directives 2008/48/EC and 2014/17/EU and Regulation (EU) No 596/2014. [↑](#footnote-ref-305)
305. [Die Achtung von Menschenrechten entlang globaler Wertschöpfungsketten (adelphi.de)](https://www.adelphi.de/de/system/files/mediathek/bilder/fb-543-achtung-von-menschenrechten-entlang-globaler-wertschoepfungsketten.pdf). [↑](#footnote-ref-306)
306. Extractive sector; Agricultural supply chains; Minerals; Garment & Footwear Sector [↑](#footnote-ref-307)
307. Based on the assumption that the scope would cover parent companies that fulfil the threshold requirements at group level. [↑](#footnote-ref-308)
308. As regards environmental harm, impacts should include, but should not be limited to, production of waste, diffuse pollution and greenhouse emissions that lead to a global warming of more than 1,5°C above pre-industrial levels, deforestation, and any other impact on the climate, air, soil and water quality, the sustainable use of natural resources, biodiversity and ecosystems. The list of human rights and environmental conventions and standards should be regularly updated through delegated acts by the Commission. [↑](#footnote-ref-309)
309. On the basis of these the Commission issued guidance regarding forced labour impacts in July 2021. [↑](#footnote-ref-310)
310. See [ILO Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy](https://www.ilo.org/wcmsp5/groups/public/---ed_emp/---emp_ent/---multi/documents/publication/wcms_094386.pdf) [↑](#footnote-ref-311)
311. See e.g. International Trade Centre (ITC): [Mapping of voluntary sustainability schemes – the Standards Map project](https://www.intracen.org/itc/market-info-tools/voluntary-standards/standardsmap/) and the Supporting study on due diligence (Table 8.8: Literature on Positive HR Impacts of Voluntary Due Diligence Approaches, p. 336). [↑](#footnote-ref-312)
312. See supporting study on due diligence, p. 243 [↑](#footnote-ref-313)
313. The EC study on due diligence requirements through the supply chain, studies commissioned by the German and Dutch governments, and by the Danish Institute for Human Rights, reached the same conclusions of a low uptake of due diligence processes by companies when done on a voluntary basis. [↑](#footnote-ref-314)
314. See in detail section 2.2.2.3. [↑](#footnote-ref-315)
315. See evidence in Section 2.1.3 and in **Annex 10** above. [↑](#footnote-ref-316)
316. Supporting study on due diligence, p. 97. [↑](#footnote-ref-317)
317. An overwhelming majority of overall respondents answering expressed support for action on a mandatory framework (660 respondents, 81.8%). Please refer for more details to Annex 2. [↑](#footnote-ref-318)
318. 40.4 % of business associations and 31.6 % of businesses contributing to the open public consultation believed an EU legal framework for supply chain due diligence was not necessary. [↑](#footnote-ref-319)
319. UN Human Rights Council, “Report of the Special Rapporteur on extreme poverty and human rights: Climate change and poverty”, A/HRC/41/39 (17 July 2019) at para 48. [↑](#footnote-ref-320)
320. [Guiding Principles On Business And Human Rights At 10: Taking stock of the first decade - Report of the Working Group on the issue of human rights and transnational corporations and other business enterprises](https://www.ohchr.org/Documents/Issues/Business/UNGPs10/Stocktaking-reader-friendly.pdf), June 2021. [↑](#footnote-ref-321)
321. See, for instance, Jeffrey, C., “[Comparing the Implementation of the EU Non-Financial Reporting Directive in the UK, Germany, France and Italy](http://www.purposeofcorporation.org/comparing-the-eu-non-financial-reporting-directive.pdf)”, Frank Bold, November 2017. [↑](#footnote-ref-322)
322. For instance the CEPS study on the NFRD ([Study on the Non-Financial Reporting Directive – CEPS](https://www.ceps.eu/ceps-publications/study-on-the-non-financial-reporting-directive/)) found some evidence of limited changes in company policies that could be partly attributed to the current requirements of the NFRD. [↑](#footnote-ref-323)
323. [EUR-Lex - 52016SC0034 - EN - EUR-Lex (europa.eu)](https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52016SC0034) [↑](#footnote-ref-324)
324. [Evaluation de la mise en œuvre de la loi n° 2017-399 du 27 mars 2017 relative au devoir de vigilance des sociétés mères et des entreprises donneuses d’ordre](https://www.vie-publique.fr/sites/default/files/rapport/pdf/275689.pdf), January 2020. [↑](#footnote-ref-325)
325. [EU Mandatory Human Rights Due Diligence Directive: Recommendations to the European Commission](https://www.ohchr.org/Documents/Issues/Business/ohchr-recommendations-to-ec-on-mhrdd.pdf), 2 July, 2021 [↑](#footnote-ref-326)
326. Shell judgment as referred to above. [↑](#footnote-ref-327)
327. [Dutch Bill on Responsible and Sustainable International Business Conduct](https://www.mvoplatform.nl/en/wp-content/uploads/sites/6/2021/03/Bill-for-Responsible-and-Sustainable-International-Business-Conduct-unofficial-translation-MVO-Platform.pdf), [Austrian proposal for a supply chain law](https://www.business-humanrights.org/en/latest-news/%C3%B6sterreich-sozialdemokraten-pr%C3%A4sentieren-vorschlag-f%C3%BCr-lieferkettengesetz/), [Belgian Vigilance proposal](https://www.lachambre.be/FLWB/PDF/55/1903/55K1903001.pdf). [↑](#footnote-ref-328)
328. UNGPs, principle 22: Where business enterprises identify that they have caused or contributed to adverse impacts, they should provide for or cooperate in their remediation through legitimate processes. [↑](#footnote-ref-329)
329. See supporting study on due diligence, Problem Analysis and Regulatory Options section. [↑](#footnote-ref-330)
330. Replies to question 19a of the open public consultation; supporting study on due diligence, p. 140. [↑](#footnote-ref-331)
331. Supporting study on due diligence, p. 155. [↑](#footnote-ref-332)
332. Reply by Hogan Lovells International LLP. [↑](#footnote-ref-333)
333. See e.g. replies from Volvo Car Corporation AB, Volkswagen Group, Federation of German Industries (BDI). [↑](#footnote-ref-334)
334. According to the report [Le radar du devoir de vigilance](https://plan-vigilance.org/wp-content/uploads/2021/07/2021-07-05-Radar-DDV-Rapport-2021.pdf) (Sherpa 2021), **6 companies** have been summoned to court or have received formal notices from organisations and/or unions. A [summary of the different cases](https://vigilance-plan.org/court-cases-under-the-duty-of-vigilance-law/) that have been introduced under the Law on the duty of vigilance is available on the [vigilance-plan.org](http://www.vigilance-plan.org/). [↑](#footnote-ref-335)
335. See e.g. [Ending child labour, forced labour and human trafficking in global supply chains](https://www.ilo.org/ipec/Informationresources/WCMS_716930/lang--en/index.htm), ILO Report, 2019; [OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas](https://mneguidelines.oecd.org/mining.htm). [↑](#footnote-ref-336)
336. A significant number of court cases dealing with companies responsibility in their value chain focused on the downstream value chain, for example depositing toxic waste (SE company Boliden depositing toxic waste in Chile which caused cancer and other diseases for decades, FR company Perenco dumping toxic products in Congo, etc). [↑](#footnote-ref-337)
337. The vast majority of greenhouse gas emissions from fossil fuels are produced by their use, when they are burned (these are so called “Scope 3” emissions according to the most widely-used international accounting tool, the Greenhouse Gas Protocol, also referenced in the Non-financial reporting Directive’s guidelines on climate disclosures). Scope 3 emissions form significant parts of many companies’ climate impacts, but for fossil fuel companies, Scope 3 emissions form the large majority of their climate impact – around 60-90% of their overall GHG emission footprint. In the Shell judgement the Court ruled that in line with the Paris Agreement’s goal of limiting global temperature rise to 1.5ºC above pre-industrial temperatures, scope 3 emissions have to be captured in due diligence. The Court found that Shell controls and influences the Scope 3 emissions of end-users by the products that it sells (see above). [↑](#footnote-ref-338)
338. See [OECD-Due-Diligence-Guidance-for-Responsible-Business-Conduct.pdf](http://mneguidelines.oecd.org/OECD-Due-Diligence-Guidance-for-Responsible-Business-Conduct.pdf), see also the [OECD’s Sectoral Guidance](http://mneguidelines.oecd.org/guidelines/), e.g. the [OECD Due Diligence Guidance for Responsible Supply Chains in the Garment & Footwear Sector](http://mneguidelines.oecd.org/responsible-supply-chains-textile-garment-sector.htm); [United Nations Guiding Principles on Business and Human Rights](https://www.ohchr.org/Documents/Publications/GuidingPrinciplesBusinessHR_EN.pdf); see e.g. commentaries to Principles 13, 17. See also the [European Parliament resolution of 10 March 2021](https://www.europarl.europa.eu/doceo/document/TA-9-2021-0073_EN.html) with recommendations to the Commission on corporate due diligence and corporate accountability (2020/2129(INL)). [↑](#footnote-ref-339)
339. See page 70 of the OECD due diligence guidance for responsible business conduct. [OECD-Due-Diligence-Guidance-for-Responsible-Business-Conduct.pdf](http://mneguidelines.oecd.org/OECD-Due-Diligence-Guidance-for-Responsible-Business-Conduct.pdf) [↑](#footnote-ref-340)
340. See [OECD-Due-Diligence-Guidance-for-Responsible-Business-Conduct.pdf](http://mneguidelines.oecd.org/OECD-Due-Diligence-Guidance-for-Responsible-Business-Conduct.pdf), p. 68 et seq., p. 75 et seq., p. 81 et seq., see also the [OECD’s Sectoral Guidance](http://mneguidelines.oecd.org/guidelines/) [↑](#footnote-ref-341)
341. The landmark Shell judgement interpreting the due diligence framework provides that Shell’s due diligence duty extends to its entire value chain, including the consumption phase: “4.4.25: it is not in dispute that through its purchase policy the Shell group exercises control and influence over its suppliers’ emissions. (…) This means that through the corporate policy of the Shell group, Royal Dutch Shell is able to exercise control and influence over these emissions. The same applies for the emissions of the product of the company: “Through the energy package offered by Shell group, Royal Dutch Shell controls and influences the Scope 3 emissions of end-users of the products produced and sold by the Shell group”. [↑](#footnote-ref-342)
342. Under the general rule of the Accounting Directive (Article 3 of [Directive 2013/34/EU](https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32013L0034&from=EN)), the limits of at least two of the three criteria mentioned in each company category must not be exceeded for a company to fall in the category: **micro**-undertakings: 10 employees / EUR 0.7 million turnover / EUR 0.35 million balance sheet total; **small** undertakings: 50 employees / EUR 8 m turnover / EUR 4 m balance sheet total; **medium-sized** undertakings: 250 employees / EUR 40 m turnover / EUR 20 m balance sheet total. An undertaking is **large** if it exceeds two of the three latter thresholds. [↑](#footnote-ref-343)
343. For the sake of completeness, human rights violations include any environmental damage, in particular harmful soil, water or air pollution, harmful noise emission or excessive water consumption, that impairs the natural basis for the preservation and production of food, denies access to safe drinking water, impedes access to sanitary facilities or harms the health of a person. See for example Section 2(2) No. 9 of the [German Supply Chain law](https://www.bgbl.de/xaver/bgbl/text.xav?SID=&tf=xaver.component.Text_0&tocf=&qmf=&hlf=xaver.component.Hitlist_0&bk=bgbl&start=%2F%2F*%5B%40node_id%3D%27910576%27%5D&skin=pdf&tlevel=-2&nohist=1). [↑](#footnote-ref-344)
344. The list includes six specific agreements creating concrete obligations that can be complied with by individual companies. All those international agreements have previously been used in EU/national legislation creating individual obligations for economic operators. [↑](#footnote-ref-345)
345. Similar interpretation has been given to the OECD due diligence framework by the Dutch National Contact Point dealing with alleged infringements of the OECD framework with respect to the absence of proper mitigation targets by a large bank (ING): in determining ING’s due diligence responsibilities, the bank was required to set targets in line with the climate neutrality goal of the Paris Agreement [↑](#footnote-ref-346)
346. Oxfam Novib, Greenpeace Netherlands, BankTrack and Friends of the Earth Netherlands (Milieudefensie) v ING [↑](#footnote-ref-347)
347. Under the EU Market Surveillance Regulation, companies selling in the single market from outside the EU have to ensure that for the products sold in the EU there is an authorised representative. The proposal for a Digital Services Act requires a point of contact and a legal representative for supervisory purposes. The proposal for a Regulation concerning batteries and waste batteries, that establishes a due diligence obligation of economic operators that place certain industrial batteries on the market, requires that a manufacturer of a battery that is not established in a Member State may only place the battery on the EU market if the manufacturer designates a sole authorised representative who is considered the economic operator. [↑](#footnote-ref-348)
348. For instance by requiring that the business partner’s interests is taken into account in directors decisions including when discharging the due diligence obligation and limiting imposition of unjustified costs in contracts, or by identifying a black list of elements that cannot be put into contracts to enforce the due diligence obligation and establishing model/standard contractual clauses (as done for the [GDPR](https://ec.europa.eu/info/law/law-topic/data-protection/international-dimension-data-protection/standard-contractual-clauses-scc_en)). [↑](#footnote-ref-349)
349. Orbis data, except for data on listed companies: CEPS study 2020 (p. 293). [↑](#footnote-ref-350)
350. Orbis data, except for data on listed companies: CEPS study 2020 (p. 293). [↑](#footnote-ref-351)
351. For what these accompanying measures could include, please see the general description of retained policy options above (other elements). [↑](#footnote-ref-352)
352. Orbis data [↑](#footnote-ref-353)
353. These could include: Helpdesks at national level; Sectorial guidelines and online tools that could be adopted by Member States; facilitating the creation of industrial alliances; capacity building (train the trainers); technology support for data sharing solutions, as well as supporting measures in producer countries, etc. [↑](#footnote-ref-354)
354. See more on this above under the description of the retained policy options (content of the due diligence obligation). [↑](#footnote-ref-355)
355. Orbis data [↑](#footnote-ref-356)
356. Orbis data [↑](#footnote-ref-357)
357. Orbis data, except for data on listed companies: CEPS study 2020 (p. 293). [↑](#footnote-ref-358)
358. For instance, in the public consultation a large majority of overall respondents answering the relevant questions expressed support or strong support for corporate directors being required by law to: identify and balance stakeholders’ interests, manage the risks for the company in relation to stakeholder interests and identify the opportunities, set up adequate procedures and measurable (science-based) targets to ensure impacts on stakeholders are addressed and integrate sustainability risks, impacts and opportunities into the company’s strategy, decisions and oversight. However, about half of the businesses disagreed with the need to clarify the need to balance stakeholder interests in legislation. For more detailed information on the results of the stakeholder consultation, please refer to Annex 2. [↑](#footnote-ref-359)
359. For example communities that would be forced to leave their natural environment or have reduced access to water or food because of the economic activity of the company. [↑](#footnote-ref-360)
360. [↑](#footnote-ref-361)
361. See also explanation in the main text of the impact assessment. [↑](#footnote-ref-362)
362. The science-based targets initiative referred to above has developed methodologies, including sectorial ones to help companies define targets aligned with climate science. [↑](#footnote-ref-363)
363. Cheema-Fox et al., 2020. The study looked at the initial stock market reaction to the COVID-19 crisis (up to 23 March 2020); see also OECD Note “COVID 19 and Responsible Business Conduct”. [↑](#footnote-ref-364)
364. European Capital Markets Institute [*ESG resilience during the Covid crisis: Is green the new gold?*](https://www.ecmi.eu/sites/default/files/ecmi_commentary_no_67_july_2020.pdf)*;* July 2020 [↑](#footnote-ref-365)
365. [Key Consumer Data 2020](https://ec.europa.eu/info/sites/info/files/120321_key_consumer_data_factsheet_en.pdf) [↑](#footnote-ref-366)
366. There is some evidence that biodiversity loss and the damage to ecosystems may encourage more rapid evolutionary processes and diversification of diseases, as pathogens spread more easily to livestock and humans. See for example Emerging Infectious Diseases of Wildlife-- Threats to Biodiversity and Human Health Peter Daszak, Andrew A. Cunningham, Alex D. Hyatt Science 21 Jan 2000: Vol. 287, Issue 5452, pp. 443-449 [↑](#footnote-ref-367)
367. [Covid-19 Is Accelerating ESG Investing And Corporate Sustainability Practices](https://www.forbes.com/sites/georgkell/2020/05/19/covid-19-is-accelerating-esg-investing-and-corporate-sustainability-practices/#1ccf955526bb); Georg Kell, founder of the UN Global Compact and Chair of asset manager Arabesque Partners. [↑](#footnote-ref-368)
368. <https://www.smart.uio.no/publications/reports/d3.1.-revised-hotspots-analysis-wp3.pdf> [↑](#footnote-ref-369)
369. TR= Turkey, whereby the denim is also partially produced in Italy, see flowchart below; VT= Vietnam; NL= Netherlands. [↑](#footnote-ref-370)
370. According to its Recital 68, “*the due diligence policies should address the risks in the battery supply chain in relation to protection of the natural environment and of the biological diversity in line with the Convention on Biological Diversity*”. [↑](#footnote-ref-371)
371. According to the Directive’s Article 18(2), “*in the performance of public contracts economic operators have to comply with applicable obligations in the fields of environmental, social and labour law established by Union law, national law, collective agreements or by the international environmental, social and labour law provisions listed in Annex X*”. [↑](#footnote-ref-372)