EUROPEAN
COMMISSION

Brussels, XXX
[…](2022) XXX draft

SENSITIVE*

Proposal for a

DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL

on Corporate Sustainability Due Diligence and amending Directive (EU) 2019/1937

(Text with EEA relevance)

* Distribution only on a 'Need to know' basis - Do not read or carry openly in public places. Must be stored securely and encrypted in storage and transmission. Destroy copies by shredding or secure deletion. Full handling instructions https://europa.eu/!db43PX

EXPLANATORY MEMORANDUM

1. CONTEXT OF THE PROPOSAL

Reasons for and objectives of the proposal

The behaviour of companies across all sectors of the economy is key to succeed in the Union's transition to a climate-neutral and green economy[1] in line with the European Green Deal[2] and in delivering on the UN Sustainable Development Goals, including on its human rights- and environment-related objectives. This requires implementing comprehensive mitigation processes for adverse human rights and environmental impacts in their supply chains, integrating sustainability into corporate governance and management systems, and framing business decisions in terms of human rights, climate and environmental impact, as well as in terms of the company's resilience in the longer term.

EU companies operate in complex surroundings and, especially large ones, rely on global value chains. Given the significant number of their suppliers in the EU and in third countries and the overall complexity of value chains, EU companies, including the large ones, may encounter difficulties to identify and mitigate risks in their value chains linked to respect of human rights or environmental impacts. Identifying these adverse impacts in value chains will become easier if more companies exercise due diligence and thus more data is available on human rights and environmental adverse impacts.

The connection of the EU economy to millions of workers around the world through global value chains comes with a responsibility to address adverse impacts on the rights of these workers. A clear request from Union citizens for the EU economy to contribute to address these adverse impacts is reflected in the existing or upcoming national legislation on human rights and environmental due diligence[3], in the debates ongoing at national level and in the call for action from the European Parliament and the Council. Both of these institutions have called on the Commission to propose EU rules for a cross-sector corporate due diligence obligation.[4] In their Joint Declaration on EU Legislative Priorities for 2022[5], the European Parliament, the Council of the European Union and the European Commission have committed to deliver on an economy that works for people, including to improve the regulatory framework on sustainable corporate governance.

---

1 Regulation (EU) 2021/1119 of the European Parliament and of the Council of 30 June 2021 establishing the framework for achieving climate neutrality and amending Regulations (EC) No 401/2009 and (EU) 2018/1999 ('European Climate Law'), which also includes a binding target to cut domestic net greenhouse gas emissions by at least 55% compared to 1990 levels by 2030.

2 Communication from the Commission on the European Green Deal, COM/2019/640 final.

3 So far France (*Loi relative au devoir de vigilance, 2017)* and Germany (*Sorgfaltspflichtengesetz, 2021)* have introduced a horizontal due diligence law, other Member States (Belgium, the Netherlands, Luxembourg and Sweden) are planning to do so in the near future, and the Netherlands has introduced a more targeted law on child labour (*Wet zorgplicht kinderarbeidm 2019)*.

4 European Parliament resolution of 10 March 2021 with recommendations to the Commission on corporate due diligence and corporate accountability (2020/2129(INL)); Council Conclusions on Human Rights and Decent Work in Global Supply Chains of 1 December 2020 (13512/20).

5 Joint declaration of the European Parliament, the Council of the European Union and the European Commission on EU Legislative Priorities for 2022 (OJ C 514I , 21.12.2021, p. 1–4).

Using the existing international voluntary standards on responsible business conduct,[6] an increasing number of EU companies are using supply due diligence as a tool to identify risks in their supply chain and build resilience to sudden changes in the supply chains, but companies may also face difficulties when considering to use the supply chain due diligence for their activities. Such difficulties can be for instance due to lack of legal clarity regarding corporate due diligence obligations, complexity of supply chains, market pressure, information deficiencies, and costs. As a consequence, the benefits of due diligence are not widespread among European companies and across economic sectors.

Mostly large companies have been increasingly deploying due diligence processes as it can provide them with a competitive advantage.[7] This also responds to the increasing market pressure on companies to act sustainably as it helps them avoid unwanted reputational risks vis-à-vis consumers and investors that are becoming increasingly aware of sustainability aspects. However, these processes are based on voluntary standards and do not result in legal certainty for neither companies nor victims in case harm occurs.

Voluntary action does not appear to have resulted in large scale improvement across sectors and, as a consequence, negative externalities from EU production and consumption are being observed both inside and outside EU. Certain EU companies have been associated with adverse human rights and environmental impacts, including in their value chains.[8] Adverse impacts include, in particular, human rights issues such as forced labour, child labour, inadequate workplace health and safety, exploitation of workers, and environmental impacts such as greenhouse gas emissions, pollution, or biodiversity loss and ecosystem degradation.

In the last years, emerging legal frameworks on corporate due diligence in Member States[9] reflect the increasing need to support companies in their endeavour to perform due diligence in their supply chains and foster business conduct that respects human rights and the environment. On the other hand, they also bring fragmentation and risk undermining legal certainty and a level playing field for companies in the single market.

An EU level legislation on corporate due diligence will advance respect for human rights and the green transition, create a level playing field for companies within the Union and would avoid fragmentation resulting from Member States acting on their own. It would also include third-country companies operating in the EU market, based on the similar turnover criterion.

---

6 United Nations' "Guiding Principles on Business and Human Rights: Implementing the United Nations 'Protect, Respect and Remedy' Framework" (2011), available at https://www.ohchr.org/Documents/Publications/GuidingPrinciplesBusinessHR_EN.pdf; OECD Guidelines for Multinational Enterprises (2011 update), available at: https://doi.org/10.1787/9789264115415-en, with set of recommendations on responsible business conduct, as well as specific OECD Due Diligence Guidance for Responsible Business Conduct (2018) and OECD sectoral guidance, available at: https://mneguidelines.oecd.org/mneguidelines/.

7 See Impact Assessment accompanying this proposal, p. 15, 23.

8 The Study on due diligence, p. 221 (see reference in footnote 66), indicates that corporate risk assessment processes continue to focus on the materiality of the risks to the company, despite international guidance (UNGPs, OECD) which clarifies that the relevant risks for due diligence must extend beyond the risks of the company to those who are affected (the rights-holders). Negative corporate impacts as a consequence of globalisation and failure to undertake due diligence, ranging from environmental disasters (see at https://www.business-humanrights.org/en/blog/brumadinho-dam-collapse-lessons-in-corporate-due-diligence-and-remedy-for-harm-done/) and land grabbing (see at https://www.europarl.europa.eu/RegData/etudes/STUD/2016/578007/EXPO_STU(2016)578007_EN.pdf) to serious violations of labour and human rights, (see at https://www.europarl.europa.eu/RegData/etudes/BRIE/2014/538222/EPRS_BRI(2014)538222_REV1_EN.pdf) are well documented.

9 See footnote 3.

Against this background, this Directive will set out a horizontal framework to foster the contribution of businesses operating in the single market to the respect of the human rights and environment in their own operations and through their value chains, by identifying, preventing, mitigating and accounting for their adverse human rights, and environmental impacts, and having adequate governance, management systems and measures in place to this end.

The Directive's specific objectives are the following:

(1) improving corporate governance practices to better integrate risk management and mitigation processes of human rights and environmental risks and impacts, including those stemming from value chains, into corporate strategies;

(2) avoiding fragmentation of due diligence requirements in the single marketand creating legal certainty for businesses and stakeholders as regards expected behaviour and liability;

(3) increasing corporate accountability for adverse impacts, and ensuring coherence for companies regarding obligations under existing and proposed EU initiatives on responsible business conduct; and

(4) improving access to remedy for those affected by adverse human rights and environmental impacts of corporate behaviour.

(5) Being a horizontal instrument focussing on business processes, applying also to the value chain, this Directive will complement other measures in force or proposed, which directly address some specific sustainability challenges or apply in some specific sectors, mostly within the EU.

Consistency with existing policy provisions in the policy area

At EU level, sustainable corporate governance has been mainly fostered indirectly by imposing reporting requirements in the Non-Financial Reporting Directive (NFRD)[10] on approximately 12 000 companies[11] concerning environmental, social and human rights related risks, impacts, measures (including due diligence) and policies.[12] The NFRD had some positive impact on improvement of responsible business operation, but has not resulted in the majority of companies taking sufficient account of their adverse impacts in their value chains.[13]

---

10 Directive 2014/95/EU amending Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups (OJ L 330, 15.11.2014, p. 1–9). The NFRD is therefore an amendment of the Accounting Directive, i.e. of Directive 2013/34/EU on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC and repealing Council Directives 78/660/EEC and 83/349/EEC (OJ L 182, 29.6.2013).

11 Large public-interest entities that have more than 500 employees (and the balance sheet total or net turnover of which exceeds the Accounting Directive's threshold for large enterprises), including listed companies, banks and insurance companies. See CEPS' Study on the Non-Financial Reporting Directive, prepared for the European Commission to support the review of the NFRD, November 2020, available at https://op.europa.eu/en/publication-detail/-/publication/1ef8fe0e-98e1-11eb-b85c-01aa75ed71a1/language-en.

12 See also some provisions of SRD II, i.e. Directive (EU) 2017/828 amending Directive 2007/36/EC as regards the encouragement of long-term shareholder engagement (OJ L 132, 20.5.2017, p. 1–25).

13 The Impact Assessment accompanying the Commission's proposal for the Corporate Sustainability Reporting Directive (SWD/2021/150 final) and the CEPS' Study on the Non-Financial Reporting Directive (section 2,) found a limited change in corporate policies as a result of the NFRD, consistent

The Commission's recent proposal for a Corporate Sustainability Reporting Directive (CSRD), revising the NFRD[14], would extend the scope of the companies covered to all large and all listed companies[15], require the audit (assurance) of reported information and strengthen the standardisation of reported information by empowering the Commission to adopt sustainability reporting standards.[16] This Directive will complement the CSRD by adding a so-called "material" corporate duty (i.e. what cope is to be covered) for some companies to perform due diligence to identify, prevent, mitigate and account for external harm resulting from adverse human rights and environmental impacts in the company's own operations and in the value chain. Of particular relevance both to value chain due diligence and directors' duties, the CSRD mandates disclosure of plans of an undertaking to ensure that its business model and strategy are compatible with the transition to a sustainable economy and with the limiting of global warming to 1.5 ℃ in line with the Paris Agreement. The two initiatives are closely interrelated and will lead to synergies. First, a proper information collection for reporting purposes under the proposed CSRD requires setting up processes, including identifying adverse impacts in accordance with the due diligence duty set up by this Directive. Second, the CSRD will cover the last step of the due diligence duty, namely the reporting stage. This Directive will lead to companies' reporting being more complete and effective. Therefore, complementarity will increase effectiveness of both measures and drive corporate behavioural change for those companies.

This Directive will also underpin the Sustainable Finance Disclosure Regulation[17] (SFDR) that has recently entered into force and applies to financial market participants (such as investment fund and portfolio managers, insurance undertakings selling insurance-based investment products and undertakings providing various pension products) and financial advisers. Under the SFDR, these undertakings are required to publish, among others, a statement on their due diligence policies with respect to principal adverse impacts of their investment decisions on sustainability factors on a comply or explain basis. At the same time, for companies with more than 500 employees the publication of such a statement is mandatory, and the Commission is empowered to adopt regulatory technical standards on the sustainability indicators in relation to the various types of adverse impacts.[18]

---

with the perception of main stakeholders who could not identify a clear pattern of change in corporate behaviour driven by these reporting rules.

14 Proposal for a Directive of the European Parliament and of the Council amending Directive 2013/34/EU, Directive 2004/109/EC, Directive 2006/43/EC and Regulation (EU) No 537/2014, as regards corporate sustainability reporting (COM/2021/189 final).

15 The sustainability reporting obligation would apply to all large companies as defined by the Accounting Directive (which the CSRD would amend) and, as of 2026, to companies (including non-EU companies but excluding all micro enterprises) listed on EU regulated markets.

16 The elaboration of draft sustainability reporting standards started in parallel with the legislative process in a project task force established by the European Financial Reporting Advisory Group (EFRAG) at the request of the Commission.

17 Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on sustainability-related disclosures in the financial services sector (OJ L 317, 9.12.2019, p. 1–16).

18 The three European Supervisory Authorities published on 4 February 2021 their Final Report (available at https://www.esma.europa.eu/press-news/esma-news/three-european-supervisory-authorities-publish-final-report-and-draft-rts) to the Commission, including the draft regulatory technical standards on disclosures under the SFDR.

Similarly, this Directive will complement the recent Taxonomy Regulation[19], a transparency tool that facilitates decisions on investment and helps tackle greenwashing by providing a categorisation of environmentally sustainable economic activities that also meet a minimum social safeguard.[20] The minimum safeguards established in Article 18 of the Taxonomy Regulation shall be procedures implemented by an undertaking that is carrying out an economic activity to ensure the alignment with the OECD Guidelines for Multinational Enterprises and the UN Guiding Principles on Business and Human Rights, including the principles and rights set out in the eight fundamental conventions identified in the Declaration of the International Labour Organization on Fundamental Principles and Rights at Work and the International Bill of Human Rights. Like the proposal for CSRD, the Taxonomy Regulation does not impose (material) duties on companies other than public reporting requirements, and investors can use such information when allocating capital to companies. This Directive by requiring companies to identify their adverse risks in all their operations and value chains may help to get more detailed information to the investors. It therefore complements the Taxonomy Regulation as it has the potential to further help investors to allocate capital to responsible and sustainable companies. Moreover, Taxonomy Regulation (as providing a common language for sustainable economic activities for investment purposes) can serve as a guiding tool for companies to attract sustainable financing for their corrective action plans and roadmaps.

This Directive will complement Directive 2011/36/EU on preventing and combating trafficking in human beings and protecting its victims[21], which constitutes a comprehensive legal framework to effectively fight all forms of exploitation in the EU by natural and legal persons, in particular forced labour, sexual exploitation, as well as begging, slavery or practices similar to slavery, servitude, or the exploitation of criminal activities, or the removal of organs. It also establishes the liability of legal persons for the offences referred to in that Directive committed for their benefit by any person who has a leading position within the legal person or the commission of the offence was possible due to the lack of supervision or control. Directive 2011/36/EU also provides for sanctions on the legal person held liable.

Furthermore, this Directive will complement the Employers' Sanctions Directive[22], which prohibits the employment of irregularly staying third-country nationals, including victims of trafficking in human beings. Employers' Sanctions Directive lays down minimum standards on sanctions and other measures to be applied in the Member States against employers who infringe upon the Directive.

This Directive will also complement existing or planned sectoral and product-related supply chain due diligence instruments at EU level due to its cross-sectoral scope and broad range of sustainability impacts covered:

---

19 Regulation (EU) 2020/852 of the European Parliament and of the Council of 18 June 2020 on the establishment of a framework to facilitate sustainable investment, and amending Regulation (EU) 2019/2088 (OJ L 198, 22.6.2020, p. 13–43).

20 The Taxonomy will be developed gradually. Minimum social safeguards apply to all Taxonomy-eligible investments, and a social dimension may be included in the future.

21 Directive 2011/36/EU of the European Parliament and of the Council of 5 April 2011 on preventing and combating trafficking in human beings and protecting its victims, and replacing Council Framework Decision 2002/629/JHA (OJ L 101, 15 April 2011, p.1)

22 Directive 2009/52/EC of the European Parliament and of the Council of 18 June 2009 providing for minimum standards on sanctions and measures against employers of illegally staying third-country nationals (OJ L 168, 30. June 2009)

The so-called Conflict Minerals Regulation[23] applies to four specific minerals and metals. It requires EU companies in the supply chain to ensure they import tin, tungsten, tantalum and gold from responsible and conflict-free sources only and put in place more specific mechanisms for conducting due diligence, e.g. an independent third-party audit of supply chain due diligence. The due diligence provisions of this Directive address also environmental impact and will apply to value chains of additional minerals that are not covered in the Conflict Minerals Regulation but produce human rights, climate and environmental adverse impacts.

The Commission's proposal for a Regulation on deforestation-free supply chains[24] focuses on certain commodities and product supply chains. It has a very specific objective, namely to reduce the impact of EU consumption and production on deforestation and forest degradation worldwide. Its requirements will, in some areas, be more prescriptive compared to the general due diligence duties under this Directive. It also includes a prohibition for placing on the market certain commodities and derived products if the requirement of "legal" and "deforestation free" cannot be ascertained through due diligence. This prohibition will apply to all operators placing the relevant products on the market, including EU and non-EU companies, irrespective of their legal form and size. Therefore, while the overall objectives of the two initiatives are mutually supportive, their specific objectives are different. This Directive will complement the Regulation on deforestation-free products by introducing a value chain due diligence related to activities that are not covered by the Regulation on deforestation-free products but might be directly or indirectly leading to deforestation and by including non-compliance under the deforestation Regulation in the civil liability regime under this Directive.

The Commission's proposal for a new Batteries Regulation[25] has the specific objectives of reducing environmental, climate and social impacts throughout all stages of the battery life cycle, strengthening the functioning of the internal market, and ensuring a level playing field through a common set of rules. It requires economic operators placing industrial or electric vehicle batteries (including incorporated in vehicles) larger than 2 kWh on the EU market to establish supply chain due diligence policies. It focusses on those raw materials of which a significant amount of the global production goes into battery manufacturing and that may pose social and environmental adverse impacts (cobalt, natural graphite, lithium, and nickel). The economic operators must submit compliance documentation for third-party verification by notified bodies and are subject to checks by national market surveillance authorities. This Directive will complement the Batteries Regulation by introducing a value chain due diligence related to raw materials that are not covered in this Regulation but without requiring certification for placing the products on the EU market.

The future Sustainable Products Initiative (SPI) aims to revise the current Ecodesign Directive[26] and concerns the sustainability of products placed on the EU market more broadly and the transparency of related information. The preparatory work on SPI considers adding more

---

23 Regulation (EU) 2017/821 of the European Parliament and of the Council of 17 May 2017 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 (OJ L 130, 19.5.2017, p. 1–20).

24 Proposal for a Regulation of the European Parliament and of the Council on the making available on the Union market as well as export from the Union of certain commodities and products associated with deforestation and forest degradation and repealing Regulation (EU) No 995/2010 (COM(2021) 706 final).

25 Proposal for a Regulation of the European Parliament and of the Council concerning batteries and waste batteries, repealing Directive 2006/66/EC and amending Regulation (EU) No 2019/1020 (COM/2020/798 final).

26 Directive 2009/125/EC of the European Parliament and of the Council of 21 October 2009 establishing a framework for the setting of ecodesign requirements for energy-related products (OJ L 285, 31.10.2009, p. 10).

specific social/human rights due diligence requirements, e.g. auditing obligations, with respect to specific products, and make compliance with such due diligence condition to place the product in EU market, should there be the need for such rules in addition to this Directive.

The provisions of the above-mentioned sector-specific Union legislative acts will provide the more specific rules (and be *lex specialis)* in relation to the due diligence duty set up by this Directive with the same objective, nature and effect. However, such specific provisions will not undermine the effective application of this Directive or the achievement of its general aim nor any aspects that are not regulated in the sector-specific Union legislative act (e.g. civil liability). The existence of specific Union rules laying down requirements regarding value chain due diligence will not exclude the application of this Directive. Where this Directive provides for more specific provisions or adds requirements to the provisions laid down in any sector-specific Union legislative act, the provisions laid down by the sector-specific Union legislative act should apply in conjunction with those of this Directive.

Consistency with other Union policies

This Directive complements existing and planned EU measures in the field of the human rights, including labour rights, and environment, and sector- and product-specific legislation setting up due diligence measures in operators' supply chains.

As part of the European Green Deal, the Commission has listed an initiative on sustainable corporate governance among the deliverables of the Action Plan on a Circular Economy, the Biodiversity strategy, the Farm to Fork strategy, the Chemicals strategy, Updating the 2020 New Industrial Strategy: Building a stronger Single Market for Europe's recovery, and the Strategy for Financing the Transition to a Sustainable Economy.

EU environmental law introduces various environmental requirements for companies, Member States, or defines goals for the EU[27]. However, it generally does not apply to value chains outside the EU where up to 80-90% of the environmental harm of EU production may occur[28]. The Environmental Liability Directive[29] establishes a framework for environmental liability with regard to prevention and remedying environmental damage based on the "polluter pays" principle for own operations. It does not cover companies' value chains.

This Directive will complement EU climate legislation, including the European Climate Law, setting in stone the EU's climate ambition, with the intermediate target of reducing net greenhouse gas emissions by at least 55% by 2030, to set Europe on a responsible path to becoming climate-neutral by 2050. Most specifically, this Directive will complement the "Fit for 55" Package[30] and its various key actions, such as setting more ambitious energy efficiency

---

27 For example it introduces limitations on the release of some pollutants, defines EU goals (such as the European Climate Law) or sets targets for Member States (such as for energy efficiency), defines obligations for Member States (e.g. on protection of natural habitats), establishes minimum content in authorisation procedures for some economic activities (e.g. Environmental Impact Assessment), etc.

28 See e.g. Jungmichel, Norbert, Christina Schampel and Daniel Weiss (2017): Atlas on Environmental Impacts - Supply Chains – Environmental Impacts and Hot Spots in the Supply Chain, Adephi/Systain, available at https://www.adelphi.de/en/system/files/mediathek/bilder/Umweltatlas%20Lieferkette%20-%20adelphi-Systain-englisch.pdf.

29 Directive 2004/35/CE of the European Parliament and of the Council of 21 April 2004 on environmental liability with regard to the prevention and remedying of environmental damage (OJ L 143, 30.4.2004, p. 56–75).

30 The "Fit for 55" Package is a series of proposals adopted by the Commission on 14 July 2021 aiming to make the EU's climate, energy, land use, transport and taxation policies fit for reducing net greenhouse gas emissions by at least 55% by 2030, compared to 1990 levels.

and renewable energy targets for Member States by 2030 or the upgrading of the EU Emissions Trading System[31], which needs to be underpinned by a wider transformation of production processes to achieve climate neutrality by 2050 across the economy and throughout value chains. The "Fit for 55" Package will only indirectly apply to some non-EU value chains of EU companies through the Carbon Border Adjustment Mechanism (CBAM)[32] which aims at preventing "carbon leakage"[33] by imposing a carbon adjustment price for selected imported products not subject to the carbon price deriving from the EU Emission Trading System.

Existing EU health and safety, and fundamental rights legislation targets very specific adverse impacts (such as violations of the right to privacy and data protection, discrimination, specific health aspects related to dangerous substances, threats to health and safety of workers, violations of rights of the child, etc.) within the EU[34] but does not cover core fundamental rights impacts and does not apply in all cases to companies' value chains outside the Union.

The initiative is in line with the EU Action Plan on Human Rights and Democracy 2020-2024[35], which includes a commitment for the EU and Member States to strengthen their engagement to actively promote the implementation of international standards on responsible business conduct such as the UN Guiding Principles on Business and Human Rights and the OECD Guidelines on Multinational Enterprises and Due Diligence. It is consistent with the EU Strategy on the Rights of the Child[36] which commits the EU to a zero tolerance approach against child labour. In the EU Strategy on Combatting Trafficking in Human Beings 2021- 2025[37] the Commission committed to put forward a legislative proposal on sustainable corporate governance to foster long-term sustainable and responsible corporate behaviour. The initiative also contributes to the goals of the Commission's Communication on decent work worldwide.

This Directive will contribute to the European Pillar of Social Rights as both promote rights such as fair working conditions[38]. It will – beyond its external angle – deal with the violation of international labour standards when they occur in the EU (e.g. forced labour cases in

---

31 Proposal for a Directive of the European Parliament and of the Council amending Directive 2003/87/EC establishing a system for greenhouse gas emission allowance trading within the Union, Decision (EU) 2015/1814 concerning the establishment and operation of a market stability reserve for the Union greenhouse gas emission trading scheme and Regulation (EU) 2015/757 (COM/2021/551 final).

32 Proposal for a Regulation of the European Parliament and of the Council establishing a carbon border adjustment mechanism (COM(2021) 564 final).

33 "Carbon leakage" resulting from the increased EU climate ambition could lead to increase total global emissions. The CBAM carbon adjustment price on selected types of imported products in the iron steel, aluminium, cement, electricity, fertilizers sectors would level the playing field between EU and imported products.

34 Under EU law, every EU worker has certain minimum rights relating to protection against discrimination based on sex, race, religion, age, disability and sexual orientation, labour law (part-time work, fixed-term contracts, working hours, informing and consulting employees). A summary is available at https://eur-lex.europa.eu/summary/chapter/employment_and_social_policy.html?root_default=SUM_1_CODED%3D17&locale=en.

35 Joint Communication to the European Parliament and the Council on the EU Action Plan on Human Rights and Democracy 2020-2024 (JOIN/2020/5 final)

36 Communication from the Commission on the EU strategy on the rights of the child (COM/2021/142 final).

37 Communication from the Commission on the EU Strategy on Combatting Trafficking in Human Beings 2021- 2025 (COM(2021) 171 final).

38 E.g. Pillar 10 of European Pillar of Social Rights on healthy, safe and well-adapted work environment and Article 7(b) International Covenant on Economic, Social and Cultural Rights (see annex of this Directive) on just and favourable conditions at work including safe and healthy working conditions.

agriculture). Therefore, internally it would also reinforce the protection of workers in the EU alongside the existing social *acquis* and contribute to prevent and tackle abuses within and across Member States.

Thus, this Directive will complement the EU's regulatory environment that currently does not include an EU-wide transparent and predictable framework that helps EU companies across all sectors of the economy to asses and manage sustainability risks and impacts across number of core human rights and environmental risks and impact areas and across their value chains too.

2. LEGAL BASIS, SUBSIDIARITY AND PROPORTIONALITY

Legal basis

The proposal is based on Article 50 and Article 114 of the Treaty on the Functioning of the European Union (TFEU).

Article 50(1) TFEU and in particular Article 50(2)(g) TFEU provide for the EU competence to act in order to attain freedom of establishment as regards a particular activity, in particular "*by coordinating to the necessary extent the safeguards which, for the protection of the interests of members and others, are required by Member States of companies or forms within the meaning of the second paragraph of Article 54 TFEU with a view to making such safeguards equivalent throughout the Union"*. This includes in particular coordination measures concerning the protection of interests of companies' shareholders and other stakeholders with a view to making such protection equivalent throughout the Union, where disparities between national rules are such as to obstruct freedom of establishment[39]. Recourse to this provision is possible if the aim is to prevent the emergence of future obstacles to the freedom of establishment resulting from the divergent development of national laws. The emergence of such obstacles must be likely and the measure in question must be designed to prevent them.[40]

This proposal regulates due diligence obligations of companies and at the same time covers – to the extent linked to due diligence – corporate directors' duties and corporate management systems to implement due diligence and thus processes and measures for the protection of the interests of members and stakeholders of the company. Several Member States have recently introduced legislation on due diligence,[41] while others are in the process of legislating or considering action[42]. Also, an increasing number of Member States have recently been regulating by requiring directors to take into account the company's external impacts[43], prioritize the interests of stakeholders in their decisions[44], or adopt a policy statement on the company's human rights strategy[45]. New and emerging laws on due diligence are considerably different despite the intention of all the Member States to build on existing international

---

39 It is recalled that as regards corporate governance measures, the EU has already legislated based on the same legal basis, e.g. Shareholders Rights Directives I and II.

40 See e.g. Case C 380/03 Germany v Parliament and Council [2006] ECR I-11573, paragraph 38 and the case-law cited.

41 See footnote 3. As regards EEA countries, Norway has adopted due diligence legislation.

42 Austria, Belgium, Denmark, Finland, Italy, Luxembourg, the Netherlands (regarding broader legislation on responsible business conduct). There are civil society campaigns in favour of introducing due diligence legislation ongoing in Ireland, Spain and Sweden. Annex 8 of the Impact Assessment accompanying this proposal provides a detailed overview on Member State/EEA laws and initiatives.

43 French *Loi Pacte*.

44 For example the Netherlands.

45 See the German *Sorgfaltspflichtengesetz*).

standards (UN Guiding Principles on Business and Human Rights OECD Responsible Business Conduct standards) and thus lead to diverging requirements. Member States may adopt legislation that is limited to specific sustainability concerns in value chains.[46] Personal scope, substantive due diligence requirements, enforcement regimes and related directors duties diverge and may do so even more in the future.[47] Other Member States can be expected to decide not to legislate in this field. Significantly different requirements among Member States thus create fragmentation of the internal market. This fragmentation is likely to increase over time.

This fragmentation risks leading to an uneven level playing field within the internal market and thus obstructing freedom of establishment. First, companies and their directors – in particular of those which have cross-border value chains – are already subject to differing requirement and will likely be subject to even more differing requirements depending on where their registered seat is located. This creates distortions of competition. Besides, some companies fall within the scope of two or more national legal frameworks dealing with sustainable corporate governance.[48] This could lead to incompatible parallel legal requirements.

The proposed measures are designed to prevent and solve such obstructions by harmonising the requirements for companies to carry out due diligence in their own operation, subsidiaries and value chain and related directors duties. They will lead to a level playing field where companies of similar size and their directors are subject to the same requirements for embedding sustainable corporate governance and corporate due diligence measures in their internal management systems and thereby protecting the interests of the company's stakeholders in a similar way. Harmonised conditions would be beneficial for cross-border operations, establishment and also investment, since it would facilitate comparison of corporate sustainability requirements and make engagement easier and thus less costly.

Article 50 TFEU is *lex specialis* for measures in order to attain freedom of establishment. In order to address the described internal market barriers comprehensively, it is here combined with the general provision of Article 114 TFEU.

Article 114 TFEU provides for the EU competence to adopt the measures for the approximation of the provisions laid down by law, regulation or administrative action in Member States which have as their object the establishment and functioning of the internal market. The EU legislature may have recourse to Article 114 TFEU in particular where disparities between national rules are such as to obstruct the fundamental freedoms or create distortions of competition and thus have a direct effect on the functioning of the internal market.

As set out above, differences between national rules on sustainable corporate governance and due diligence obligations are due to have a direct impact on the functioning of the internal market. Beyond the freedom of establishment, the products of companies, including third-country companies which do not comply with national due diligence rules are more likely to flow to Member States with no due diligence regimes, substantially impacting the flow of products and services. Moreover, companies supplying goods or services, in particular SMEs,

---

46 For instance, the Dutch law referred to above sets up horizontal mandatory due diligence for child labour concerns through the whole value chain. In Austria, a political party referred a draft bill on social responsibility regarding forced and child labour in the garment sector.

47 The French *Loi relative au devoir de vigilance* and the German *Sorgfaltspflichtengesetz* differ considerably in terms of personal scope material requirements and enforcement regime.

48 For instance, pursuant to the German *Sorgfaltspflichtengesetz*, any company with a branch office and at least 3000 employees in Germany (1000 as from 2024) fall within the scope of the law.

will be confronted with different rules and expectations from customers located in different EU Member States.

It is foreseeable that these distortions and impacts would become more serious with time as more and more Member States will adopt diverging national laws or may even lead to a race to the bottom in forthcoming due diligence legislations.

Distortions are also relevant for civil liability in case of harm caused in a company's value chain. Some national legal frameworks on due diligence include an express civil liability regime linked to the failure to execute due diligence, others expressly exclude a specific civil liability regime.[49] A number of companies have been brought before courts for causing or failing to prevent adverse impacts at the level of their subsidiaries or value chain. Such cases are judged based on differing rules today, as also explained above. In the absence of common rules, substantial national liability regimes may lead to different judgements depending on whether there is an ownership control (as regards subsidiaries) or factual control situations (through a) direct contracts or b) where control could be exercised by the company (through contractual cascading or other leverage in indirect relationships). This fragmentation would distort the level playing field in the internal market as a company located in one Member State would be subject to damages claims due to harm caused in its value chain whilst a company with the same value chain would be exempt from this financial and reputational risk because of diverging national rules.

The proposed civil liability regime would clarify which rules apply in case harm occurs in a company's own operation, subsidiaries and at the level of the value chain. In addition, the proposed provision on applicable law serves the purpose of ensuring application of the harmonised rules, including on civil liability, also in cases where otherwise the law applicable to such claim is not the law of a Member State, it is therefore accessory to the measures put forward under this directive under the above mentioned legal basis.

Subsidiarity

First, Member States' legislation alone in the area is unlikely to be sufficient and efficient. As regards specific transboundary problems, such as pollution, climate change, biodiversity etc. individual action is hampered by the inaction of other Member States. The achievement of international commitments such as the goals of the UNFCCC[50]'s Paris Agreement on climate change and the Glasgow Climate Pact, the Convention on Biological Diversity, as well as other multilateral environmental agreements by individual Member State action alone is unlikely. Furthermore, risks resulting from adverse human rights and environment impacts present in companies' value chains have often cross-border effects (e.g. pollution, transnational supply and value chains).

Second, many companies are operating EU-wide or globally; value chains expand to other EU Member States and increasingly to third countries. Institutional investors which invest across the borders own a large part (38%[51]) of the total market capitalisation of large European listed companies, therefore many companies have cross-border ownership and their operations are

---

49 The French *loi relative au devoir de vigilance* includes a provision on civil liability. The German *Sorgfaltspflichtengesetz* clarifies that a violation of an obligation under the law does not give rise to any civil liability while general liability rules remain unaffected. Moreover national civil liability legislations are not harmonized.

50 United Nations Framework Convention on Climate Change

51 This number comes from the Impact Assessment of the Shareholders Rights Directive II.

influenced by regulations in some countries or lack of action in others. This is one of the reasons why frontrunner companies arguably cannot go as far as they would want to in addressing sustainability issues including those in the value chains today[52] and ask for a cross-border level playing field.

Third, companies operating across the single market and beyond need legal certainty and a level-playing field for their sustainable growth. Some Member States have recently introduced legislation on due diligence[53], while others are in the process of legislating or considering action[54]. Existing Member State rules and those under preparation do have or would most likely lead to diverging requirements, which risks being inefficient and leading to an uneven playing field. There are considerable indirect effects of diverging due diligence laws on the suppliers that supply to different companies falling under different laws, as the obligations are in practice translated into contractual clauses. If due diligence requirements are significantly different among Member States, this creates legal uncertainty, fragmentation of the Single market, additional costs and complexity for companies and their investors operating across borders as well as other stakeholders. EU action can avoid this and therefore has added value.

Finally, compared to individual action by Member States, EU intervention can ensure a strong European voice in policy developments at the global level[55].

Proportionality

The burden on companies stemming from compliance costs, has been adapted to the size, resources available, and the risk profile. For that purpose the material and personal scope, and enforcement were restricted as further explained below.

As regards the "personal scope" of the due diligence obligations (i.e. which business categories are covered), small and medium sized enterprises (SMEs) that include micro companies and overall account for around 99 % of all companies in the Union, are excluded from the due diligence duty. For this category of companies, the financial and administrative burden of setting up and implementing a due diligence process would be relatively high. For the most part, they do not have pre-existing due diligence mechanisms in place, they have no know-how, specialised personnel, and the cost of carrying out due diligence would impact them disproportionately. They will, however, be exposed to some of the costs and burden through business relationships with companies in scope as large companies are expected to pass on demands to their suppliers. Hence, supporting measures will be necessary to help SMEs build operational and financial capacity. At the same time, exposure of an individual SME to adverse sustainability impacts will as a general rule be lower than the exposure of larger companies.

---

52 E.g. food producer Danone has recently been forced to cut costs by investors on grounds of lack of short-term profitability, see article *Can Anglo-Saxon activist investors whip Danone into shape?*, available at https://www.economist.com/business/2021/02/20/can-anglo-saxon-activist-investors-whip-danone-into-shape.

53 See footnote 3.

54 See footnote 42.

55 In 2014, the UN Human Rights Council decided to establish an open-ended intergovernmental working group (OEIGWG) on transnational corporations and other business enterprises with respect to human rights, whose mandate shall be to elaborate an international legally binding instrument (LBI) to regulate, in international human rights law, the activities of transnational corporations and other business enterprises. In 2021, the OEIGWG released a third revised draft LBI on business activities and human rights, including due diligence measures and corporate liability for human rights abuses.

Therefore, very large companies[56] will be within the scope of the full due diligence obligation, also because many of them have already certain processes in place e.g. because of reporting. In particular, the selected turnover criteria will filter those having the largest impact on the EU economy. Moreover, this Directive lays down measures to limit the passing on of the burden from those large companies to the smaller suppliers in the value chain.

As far as companies with lower turnover and less employees[57] are concerned, the due diligence obligation is limited to larger midcap companies active in particularly high-impact sectors that are at the same time covered by existing sectoral OECD guidance[58]. This limitation aims to create a balance between the interest in achieving the goals of the Directive and the interest in minimising the financial and administrative burden on companies. The due diligence obligation for these companies will be simplified as they would only focus on severe adverse impacts and to identify their severe adverse impacts in a way that is commensurate to the complexity of their value chains, sectors, products or the geographical regions. Moreover the due diligence obligation will apply to them only 3 years after the end of the transposition period for this Directive allowing to establish the necessary processes and procedures and benefit from industry cooperation, technological developments, standards, etc. that are likely to be prompted by the earlier implementation date for larger companies. Other companies of the same size will still be subject to transparency and reporting under the CSRD allowing them to develop due diligence policies targeted to their needs and capacity and to learn from experience of the larger companies.

To the extent that this Directive also covers third-country companies, the criteria used for defining the scope of EU and non-EU companies covered are not the same: for third-country companies, a net turnover threshold is used (EUR 150 million for group 1 and EUR 40 million for group 2), but all of this turnover needs to be generated in the EU. EU companies, in turn, have to have a net turnover of EUR 150 million generated worldwide and have to fulfil an employee criterion as well (above 500 employees in group 1 and above 250 employees in group 2). Such difference in the criteria used is justified for the following reasons:

– The EU turnover criterion for third-country companies creates a link to the EU. Including only turnover generated in the EU is justified since such a threshold, appropriately calibrated, creates a territorial connection between the third-country companies and the EU by the effects that the activities of these companies may have on the EU internal market, which is sufficient for EU law to apply to third-country companies.

– Also, the Country-by-Country Reporting Directive – an amendment to the Accounting Directive – has already established the methods for calculating net turnover for non-EU companies, while such methodology does not exist for calculating the number of employees of third-country companies. The experience with the French law regulating due diligence shows that, in the absence of a common definition of an employee, the

---

56 Large limited liability companies with more than 500 employees and a net turnover of more than EUR 150 million.

57 Large limited liability companies with more than 250 employees and a net turnover of more than EUR 40 million but not simultaneously exceeding both the 500 employee and the net turnover EUR 150 million net turnover thresholds, as well as third-country companies of a comparable legal form with a net EU turnover of EUR 40 to 150 million.

58 The OECD developed such sectoral guidance in order to promote the effective observance of OECD Guidelines on Multinational Enterprises. See the list of sectoral guidance documents at: http://mneguidelines.oecd.org/sectors/.

number of employees (worldwide) is difficult to calculate, which hinders the identification of which third-country companies are covered by the scope, preventing effective enforcement of the rules.

– Using both employee and turnover criteria for EU companies would ensure better alignment with the Corporate Sustainability reporting Directive which is used for the reporting of due diligence measures and policy for EU companies.

– While the Directive will cover about 13 000 EU companies[59], based on the estimations of the Commission, it will only cover about 4 000 third-country companies[60]. The fact that EU companies will only be covered if they also reach the minimum limit on the number of employees is very unlikely to change the conditions of competition in the EU internal market: the two size criteria applicable to EU companies, even if cumulative, will result in still covering relatively smaller companies compared to non-EU companies due to the fact that, in their case, the entire worldwide net turnover of the company is to be taken into account.

Finally, large third-country companies having a high turnover in the EU have the capacity to implement due diligence and will benefit from the advantages coming with due diligence also in their operations elsewhere. In all other aspect, third-country companies are covered by the due diligence rules the same way as their EU counterparts (for example as regards the regime applicable to companies operating in high-impact sectors and identical phase in period for those companies). The harmonisation of the duties of directors is limited to EU companies only, thus third-country companies will have more restricted obligations.

Effective enforcement of the due diligence duty is key to achieving the objectives of the initiative. The Directive will provide for a combination of sanctions and civil liability.

As regards private enforcement through civil liability different approach is used for company`s own operation and its subsidiaries and it has been restricted for the business relations. In particular, it concerns only established business relationships with which a company has regular, lasting and frequent cooperation and applies only where the adverse impact could have been foreseen, prevented, ceased or mitigated with appropriate due diligence measures. Civil liability is particularly important in enabling victims to obtain a remedy for a damage. However, it will in practice be difficult to prevent all risks through global value chains. Liability is therefore limited to harm done in the value chain under specific conditions especially beyond established direct suppliers. This approach to civil liability will also limit the risk of affluence of litigation cases.

The measures related to public enforcement of the due diligence duty do not go beyond what is necessary either. The power of public authorities to supervise and impose proportionate pecuniary sanctions in case of non-compliance is key to an effective enforcement regime.

Furthermore, this Directive does not entail unnecessary costs for the Union, national governments, regional or local authorities. The Directive will leave it up to the Member States how to organise enforcement. Administrative supervision can be carried out by existing authorities. To reduce the costs (for instance when supervising third-country companies active in various Member States) and improve the supervision, coordination, investigation and exchange of information the Commission will set up a European Network of Supervisory Authorities.

---

59 In group 1: 9 400 companies, in group 2: 3 400 companies.

60 In group 1: 2 600 companies, in group 2: 1 400 companies. The methodology used for calculating the number of third-country companies is explained in the accompanying Staff Working Document.

Choice of the instrument

The proposed instrument is a Directive, since Article 50 TFEU is the legal basis for company law legislation regarding the protection of the interests of companies' members and others with a view to making such protection equivalent throughout the Union. Article 50 TFEU requires the European Parliament and the Council to act by means of directives.

In order to provide support to companies and to Member State authorities on how companies should fulfil their due diligence obligations, the Commission, in consultation with the European Union Agency for Fundamental Rights, the European Environment Agency, the Executive Agency for Small and Medium-sized Enterprises, and where appropriate with international bodies having expertise in due diligence implementation, may issue guidelines, where necessary. Guidelines may also be used to help companies identify the severe adverse impacts in each of the high-impact sectors covered and additional Commission Guidelines may outline model contractual clauses that companies can use when cascading the obligation in their value chain and may provide harmonised methodology on the alignment of industrial schemes and multi-stakeholder initiatives.

In addition to the Guidelines the Commission may put in place other supporting measures building on existing EU actions and tools to support due diligence implementation within the Union and in third countries and devising new measures, including facilitation of joint stakeholder initiatives to help companies fulfil their obligations and support SMEs impacted by this Directive in other ways. This may be further complemented by EU development cooperation instruments to support third country governments and upstream economic operators in third countries addressing adverse human rights and environmental impacts of their operations and upstream business relationships.

3. RESULTS OF EX-POST EVALUATIONS, STAKEHOLDER CONSULTATIONS AND IMPACT ASSESSMENTS

Stakeholder consultations

In line with the better regulation guidelines, several consultation activities have taken place:

– The inception impact assessment (roadmap), which received 114 feedbacks;

– The open public consultation[61], which received 473 461 responses and 122.785 citizen signatures, , the vast majority of which were submitted through campaigns using pre-filled questionnaires, and 149 position papers;

– A dedicated consultation of social partners;

– 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); and

– Conferences and meetings with business associations, individual businesses, including Small and Medium-sized Enterprises (SMEs) representatives, civil society, including

[61] Summary of the open public consultation for the initiative on sustainable corporate governance, available at https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12548-Sustainable-corporate-governance/public-consultation_en.

non-governmental and not-for-profit organisations, as well as international organisations, such as OECD.

Overall, the consultation activities showed that there is generally a wide acknowledgement among stakeholders of the ***need for an EU legal framework for due diligence***.[62] In particular, large companies across the board asked for greater harmonisation in the area of due diligence to improve legal certainty and create a level playing field. Citizens and civil society associations perceived the current regulatory framework as ineffective to ensure corporate accountability for negative impacts on the human rights and environment.

A vast majority of respondents to the open public consultation, including most participating Member States, were in favour of a horizontal approach to due diligence over a sector-specific or thematic approach[63]. Companies indicated that they feared the risk of competitive disadvantages vis-à-vis third-country companies that do not have the same duties. Accordingly, most respondents agreed that due diligence rules should also apply to third-country companies which are not established in the EU but carry out activities of a certain scale in the EU[64].

Regarding an enforcement mechanism accompanying a mandatory due diligence duty, all stakeholder groups responding to the open public consultation indicated by a majority that supervision by competent national authorities with a mechanism of EU cooperation/coordination is the most suited option.[65]

A majority of respondents in all stakeholder groups considered binding rules with targets to be the option entailing the most costs, but also the most benefits overall. Although most respondents saw the positive impact on third countries, a subset of respondents fear a potential negative impact of due diligence rules on third countries if companies investing in third countries with weak human rights, including social and labour, and environmental protection, would have to withdraw from these countries.

Detailed information on the consultation strategy and conclusions of the stakeholder consultations can be found in Annex 2 of the impact assessment report.

Collection and use of expertise

To support the analysis of the different options, the Commission awarded support contracts to external experts for a study on due diligence requirements through the supply chain[66] and for a study on directors' duties and sustainable corporate governance[67]. These experts worked in close cooperation with the Commission throughout the different phases of the study.

---

62 For instance, in response to the open public consultation, NGOs supported the need for action with 95.9%, companies with 68.4% (large companies with 75.5%, SMEs with 58.7 %) and business associations with 59.6 %.

63 While 97.2% of NGOs preferred a horizontal approach, overall companies did so with 86.8%, including SMEs (81.8%), as well as business association (85.3%). This is true also for Member States respondents.

64 97 % of respondents agreed to this statement (NGOs 96.1%, business associations 96.5%, companies 93.8%, including SMEs 86.4%). All Member State respondents agree with this statement as well.

65 It 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%).

66 European Commission, Directorate-General for Justice and Consumers, Torres-Cortés, F., Salinier, C., Deringer, H., et al., Study on due diligence requirements through the supply chain: final report, Publications Office, 2020, https://data.europa.eu/doi/10.2838/39830

67 European Commission, Directorate-General for Justice and Consumers, Study on directors' duties and sustainable corporate governance: final report, Publications Office, 2020, https://data.europa.eu/doi/10.2838/472901. https://data.europa.eu/doi/10.2838/472901.

Besides these support studies, additional expertise was identified through literature research and through the stakeholder consultation responses.

Alongside the above-mentioned support studies, expert group meetings, and stakeholder consultations, the Commission also paid close attention to the relevant European Parliament resolution and to the Council Conclusions. The European Parliament resolution of 10 March 2021 provided recommendations to the Commission on corporate due diligence and corporate accountability, calling upon the Commission to propose EU rules for a comprehensive corporate due diligence obligation. The Council Conclusions on Human Rights and Decent Work in Global Supply Chains of 1 December 2020 called upon the Commission to table a proposal for an EU legal framework on sustainable corporate governance, including cross-sector corporate due diligence obligations along global supply chains.

Impact assessment

The analysis in the impact assessment addressed in a broad sense the problem arising from the need to reinforce sustainability in corporate governance and management systems, with two dimensions: (1) stakeholder interests and stakeholder-related (sustainability) risks to companies are not sufficiently taken into account in corporate risk management systems and decisions; (2) companies do not sufficiently mitigate their adverse human rights and environmental impacts, do not have adequate governance, management systems and measures to mitigate their harmful impacts.

After consideration of different policy options mainly in the areas of corporate due diligence duty and directors' duties, the impact assessment proposed a preferred package of policy options across three elements: corporate due diligence, directors' duties and remuneration, which complement each other.

The draft impact assessment was submitted to the Commission's Regulatory Scrutiny Board on 9 April 2021. Following the negative opinion by the Board, a revised impact assessment was submitted to the Board for a second opinion on 8 November 2021. While noting the significant revision of the report in response to the Board`s first opinion, the Board nevertheless issued a second negative opinion on 26 November 2021[68], which underlined the need for political guidance on whether, and under which conditions, the sustainable corporate governance initiative could proceed further. The Board maintained its negative opinion because it considered that the impact assessment report did not sufficiently (1) address the problem description and provide convincing evidence that EU businesses, in particular SMEs, do not already sufficiently reflect sustainability aspects or do not have sufficient incentives to do so; (2) present a scope of policy options and identify or fully assess key policy choices; (3) assess the impacts in a complete, balanced and neutral way and reflect uncertainty related to the realisation of benefits, and (4) demonstrate the proportionality of the preferred option.

Therefore, in order to address the comments of the Board's second negative opinion, the impact assessment is complemented by a staff working document on the follow-up of the Board's opinion that provides additional clarifications and evidence on the areas where the Board had provided specific suggestions of improvements.

According to the Commission's Better Regulation rules a positive opinion from the Regulatory Scrutiny board is required for a file to proceed to the adoption stage. However, the Vice President for Inter-Institutional Relations and Foresight can allow for the continuation of the preparations for an initiative that has been subject to a second negative opinion by the Regulatory Scrutiny Board. It is important to flag that the opinions of the Regulatory scrutiny

[68] Insert link to RSB opinions

Board are an assessment of the quality of the impact assessment and not an assessment of the related legislative proposal.

The Commission, also in the light of the agreement by the Vice-President for Inter-Institutional Relations and Foresight, has considered it opportune to proceed with the initiative for the following reasons:

– the *political importance* of this initiative for the Commission's political priority of "An economy that works for people", including within the context of the Sustainable Finance package and the European Green Deal and

– the *urgency of action* in the field of value chain due diligence as contribution to the sustainability transition, and to address the risk of the increasing Single market fragmentation, as well as the view that

– the *additional clarification and evidence* provided satisfactorily addressed the shortcomings of the impact assessment identified by the Regulatory Scrutiny Board and were considered in the adapted legal proposal.

With regard to its importance and urgency, the Commission also took note that the initiative was included in the Joint Political Priorities for 2022 by the European Parliament, the Council and the Commission.

After careful analysis of the Board's findings and considering the reflections on the additional clarifications and evidence provided, the Commission considers that the proposal, which has been significantly revised as compared to the package of policy options put forward by the impact assessment, allows still to decisively move forward towards the overall objective to better exploit the potential of the single market to contribute to the transition to a sustainable economy and to foster long-term sustainable and responsible corporate behaviour. The Directive is more focused and targeted compared to the preferred option outlined in the draft impact assessment. The core of it is the due diligence obligation, while significantly reducing directors' duties by linking them closely to the due diligence obligation. In addition, the scope of due diligence is adapted. A detailed description of the adaptations made to the preferred option package of the impact assessment can be found in the accompanying Staff Working Document that presents the follow-up to the opinion of the Regulatory Scrutiny Board and additional information.

In short, the "personal scope" i.e. which business categories are covered has been significantly reduced following reflections triggered by the Board's comments on the problem description, in particular with regard to SMEs, and on the proportionality of the preferred option. Concretely, SMEs have been completely excluded, from the scope, and the coverage of high-impact sectors has been shifted only to companies having more than 250 employees and more than EUR 40 million turnover (while large companies which simultaneously exceed both the 500 employee and the EUR 150 million net turnover limits are covered by the scope irrespective of their sectors of economic activities. The high-impact sectors are directly defined in the text, thus also reflecting on the Board's comments as regards legislative technique. The definition of high-impact sectors has been limited to sectors with high risk of adverse impacts and for which OECD guidance exists. For midcap companies in high-impact sectors, the rules will start to apply after a transition period of three years to allow for a longer adaptation period. In addition, the due diligence obligations of these companies are limited to severe impacts only.

To reach the objectives of the initiative effectively, the scope of this proposal extends to companies from third countries. Only such non-EU companies are covered which have a direct link to the EU market, and which have similar legal forms and meet the similar turnover

threshold as EU companies. Furthermore, they will face the same obligations regarding due diligence as the respective EU companies.

The Directive also indicates that accessible and practical support is necessary for companies, in particular SMEs in the supply chain, to prepare for the obligations (or the consequent demands the may be passed on to them indirectly). This could include practical guidance and supporting tools such as hotlines, databases or training, as well as the setup of an observatory to help companies with the implementation of the directive. Moreover, the review clause makes explicit reference to the personal scope of the Directive (i.e. coverage of business categories), which should be reviewed in light of the practical experiences with the application of the legislation.

As regards the material scope (i.e. what is covered), a cross-cutting instrument covering human rights and environmental impacts has been retained. This reflects the strong consensus amongst stakeholder groups that a horizontal framework is necessary to address the identified problems.

Furthermore, the Board commented that the impact assessment is not sufficiently clear about the need to regulate directors' duties on top of due diligence requirements. The Commission therefore decided to address this issue by deviating from the preferred options' package in the impact assessment and focussing on the directors' duties element, in light of the existing international standards[69], on due diligence. This encompasses directors' duties relating to the setting up and overseeing the implementation of corporate due diligence processes and measures as well as embedding due diligence into the corporate strategy. In order to fully reflect the role of directors in light of the corporate due diligence obligations, the directors' general duty of care for the company, which is present in the company law of all Member States, is also being clarified, to cover that directors should manage the company taking into account human rights, climate and environmental matters inherent in its activities. The proposal further provides for selected specific duties as part of the directors' duty of care, in particular relating to identifying risks to the company's operations and related to sustainability matters, including, where applicable, climate change, to adopting a plan for the transition to a sustainable economy and with the limiting of global warming to 1.5 ℃ in line with the Paris Agreement. Further reaching specific directors' duties that had been put forward in the impact assessment are not retained. This will ensure that the proposal delivers on its objective while remaining proportionate.

With regard to comments of the Board, this Explanatory Memorandum as well as the recitals of the legislative proposal contain comprehensive explanations of the policy choices made. While the impact assessment submitted to the Board and the Board's opinion have been published unchanged, a separate accompanying Staff Working Document has been prepared to provide additional evidence and clarifications that follows up on the Board's remarks including as regards evidence. This document addresses in particular the following:

1. Problem description:

– the scale and evolution of the environmental and sustainability problems directly linked to the apparent absence or insufficient use of corporate sustainability management practices by EU companies to be tackled by this Directive and the added value of the Directive in relation to the comprehensive package of measures to promote sustainability under the Green Deal;

– why the market and competitive dynamics together with the further evolution of companies' corporate strategies and risk management systems are considered

[69] See footnote 6.

insufficient and as regards the assumed causal link between using corporate sustainability tools and their practical effect in tackling the problems;

2. Impacts of the preferred option:

– issues related to third countries, integrating observations (i) on expected developments in third countries (including taking into account EU and international trade and development support measures), (ii) on impacts on third countries and on suppliers in third countries;

– the enforcement mechanism, further expanding on the added value of a two-pillar enforcement system that builds on administrative enforcement and civil liability;

– impacts on competition and competitiveness.

Regulatory fitness and simplification

Small and medium-sized enterprises, including micro enterprises are not included in the scope and indirect effects on them will be mitigated through supporting measures and guidelines at EU and Member State level as well in business to business relations with the use of model contractual clauses and by proportionality requirements for the larger business partner.

Fundamental rights

As explained in the impact assessment and based on existing evidence, mandatory due diligence requirements can have significant benefits for the protection and promotion of fundamental rights.

4. BUDGETARY IMPLICATIONS

There are no direct implications to the EU budget.

5. OTHER ELEMENTS

Implementation plans and monitoring, evaluation and reporting arrangements

The Commission will set up a European Network of Supervisory Authorities to help with the implementation of this Directive. Such Network will be composed by the representatives of the supervisory authorities designated by the Member States to ensure compliance by the companies of their due diligence obligations, in order to facilitate and ensure the coordination and convergence of regulatory, investigative, sanctioning and supervisory practices, and the sharing of information among these supervisory authorities.

After five [seven] years following the end of the transposition period, the Commission shall report on the implementation of this Directive, including, among other aspects, its effectiveness. The report shall be accompanied, if appropriate, by a legislative proposal.

In order to provide clarity and support to companies and Member States with the implementation of the directive, the Commission will issue guidance, where necessary.

Explanatory documents

To ensure the proper implementation of this Directive, the explanatory document, e.g. in the form of correlation tables would be necessary.

Detailed explanation of the specific provisions of the proposal

Article 1 sets out the subject matter of the Directive, i.e. laying down rules on obligations of due diligence by companies regarding actual and potential human rights and environmental adverse impacts, with respect to their own operations, the operations of their subsidiaries, and the value chain operations carried out by established business relationships; the provision also specifies that this Directive establishes rules on liability for violations of the due diligence obligation.

Article 2 establishes the personal scope of application of the Directive and sets out the criteria based on which a Member State is competent to regulate matters covered in this Directive.

Article 3 contains definitions for the purpose of this Directive.

Article 4 requires Member States to ensure that companies conduct human rights and environmental due diligence by complying with the specific requirements listed in Articles 5 to 10 of the Directive.

Article 5 requires Member States to ensure that companies integrate due diligence into all corporate policies and have in place a due diligence policy that is updated and published annually. The provision specifies that this policy should include a description of the company's approach, including in the long term, to due diligence as well a code of conduct describing rules and principles to be followed by the company's employees and subsidiaries as well as a description of the processes put in place to implement due diligence.

Article 6 establishes the obligation for Member States to ensure that companies take appropriate measures to identify actual or potential adverse human rights and environmental impacts in their own operations, in their subsidiaries and at the level of their established direct or indirect business relationships in their value chain.

Article 7 sets out the requirement for Member States to ensure that companies take appropriate measures to prevent potential adverse impacts identified pursuant to Article 6, or to minimise those impacts, where prevention is not possible or requires gradual implementation.

Article 8 establishes the obligation for Member States to ensure that companies take appropriate measures to bring to an end actual adverse human rights and environmental impacts that they had or could have identified pursuant to Article 6. Where an adverse impact that has occurred at the level of established direct or indirect established business relationships cannot be brought to an end, Member States should ensure that companies minimise the extent of the impact.

Article 9 sets out the obligation for Member States to ensure that companies provide for the possibility to submit complaints to the company in case of legitimate concerns regarding those potential or actual adverse impacts, including in the company's value chain. Companies are required to grant this possibility to persons who are affected or have reasonable grounds to believe that they might be affected by an adverse impact, to trade unions and other workers' representatives representing individuals working in the value chain concerned, and to civil society organisations active in the area concerned.

Article 10 introduces the obligation for Member States to require companies to periodically assess the implementation of their due diligence policy in order to verify that adverse impacts are properly identified and that preventive or corrective measures are implemented, and to determine the extent to which adverse impacts have been prevented, brought to an end or their extent minimised.

Article 11 establishes the obligation for Member States to ensure that companies as defined in Article 2(2) shall publish an annual statement in line with the reporting requirements under Directive 2013/34/EU as amended by the Corporate Sustainability Reporting Directive.

Article 12 sets out the obligation for the Commission to adopt guidance about non-binding model contract clauses to help companies comply with Article 7(2), point (b), and Article 8(3) point (c).

Article 13 sets out the possibility for the Commission, in order to provide support to companies or to Member State authorities on how companies should fulfil their due diligence obligations, to issue guidelines, for specific sectors or specific adverse impacts, in consultation with the European Union Agency for Fundamental Rights, the European Environment Agency, the European Innovation Council and Small and Medium-sized Enterprises Executive Agency, and where appropriate with international bodies having expertise in due diligence.

Article 14 requires the Member States and Commission to provide accompanying measures to companies in the scope of this Directive actors and to actors along global supply chains that are indirectly impacted by the obligations of the Directive. Such support can range from the operation of dedicated websites, portals or platforms to financial support to SMEs, and facilitation of joint stakeholder initiatives. This provision further clarifies that companies may rely on industry schemes and multi-stakeholder initiatives to support the implementation of due diligence and that the Commission, in collaboration with Member States, may issue guidance for assessing the fitness of such schemes.

Article 15 introduces the requirement for companies formed in accordance with the legislation of a third country and falling within the scope of application of the present Directive pursuant to Article 2(2), to designate a sufficiently mandated authorised representative in the Union to be addressed by Member States' competent authorities, on all issues necessary for the receipt of, compliance with and enforcement of legal acts issued in relation to this Directive.

Article 16 sets out the requirement for Member States to designate one or more national supervisory authorities in order to ensure compliance by companies of their due diligence obligations and to exercise the powers of enforcement of those obligations in accordance with Article 17.

Article 17 sets out the appropriate powers and resources of the supervisory authorities designated by the Member States to carry out their tasks of supervision and enforcement.

Article 18 establishes the requirement for Member States to ensure that any natural or legal person that has reasons to believe, on the basis of objective circumstances, that a company does not appropriately comply with the provisions of this Directive, is entitled to submit substantiated concerns, in particular in the Member State of his or her habitual residence, registered office, place of work or place of the alleged infringement, to the supervisory authorities.

Article 19 sets out that Member States shall lay down rules on sanctions applicable to infringements of the national provisions adopted pursuant to this Directive, and shall take all measures necessary to ensure that they are implemented. The sanctions shall be effective, dissuasive and proportionate. Member States shall ensure that decision of the supervisory authorities containing sanctions related to the breach of the provisions of this directive should be published.

Article 20 introduces a European Network of Supervisory Authorities composed by the representatives of the supervisory national authorities referred to in Article 16, with the aim to facilitate and ensure the coordination and alignment of regulatory, investigative, sanctioning and supervisory practices, and the sharing of information among these supervisory authorities.

Article 21 sets out the requirement for Member States to lay down rules governing the civil liability of the company for damages arising due to its failure to comply with the due diligence obligations under specific conditions. It also introduces the obligation for Member States to

ensure that the liability provided for in paragraphs 1 to 3 of this Article is not denied on the sole ground that the law applicable to such claims is not the law of a Member State.

Article 22 establishes the application of Directive (EU) 2019/1937 of the European Parliament and of the Council of 23 October 2019 on the protection of persons who report breaches of Union law, to the reporting of all breaches of this Directive and the protection of persons reporting such breaches.

Article 23 clarifies the need for compliance with due diligence obligations for the purpose of public procurement in line with the relevant provisions of Directive 2014/24/EU, Directive 2014/25/EU and Directive 2014/23/EU.

Article 24 clarifies directors' duty of care and stipulates some specific directors' duties as part of the directors' duty of care, in particular relating to identifying risks to the company's operations and related to sustainability matters, including, where applicable, climate change, to adopting a plan for the transition to a sustainable economy and with the limiting of global warming to 1.5 °C in line with the Paris Agreement.

Article 25 lays down the duty for directors of companies as defined in Article 2(1) to set up and oversee the implementation of corporate sustainability due diligence processes and measures and to adapt the corporate strategy to due diligence.

Article 26 amends the Annex of Directive (EU) No 2019/1937.

Article 27 sets out the committee procedure and establishes a committee to assist the Commission.

Article 28 contains a provision on the review of this Directive.

Article 29 contains provisions on the transposition of the Directive.

Article 30 sets the date of when this Directive enters into force.

Article 31 sets out the addressees of this Directive.

The lists contained in the Annex specify the adverse environmental impacts and adverse human rights impacts relevant for this Directive. To cover the violation of rights and prohibitions including the international human rights agreements (Part I.A), human rights and fundamental freedoms conventions (Part I.B), and the violation of internationally recognised objectives and prohibitions included in the environmental conventions (Part II).

Proposal for a

DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL

on Corporate Sustainability Due Diligence and amending Directive (EU) 2019/1937

(Text with EEA relevance)

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Articles 50(1) and 114(1) thereof,

Having regard to the proposal from the European Commission,

After transmission of the draft legislative act to the national parliaments,

Having regard to the opinion of the European Economic and Social Committee[70],

Acting in accordance with the ordinary legislative procedure,

Whereas:

(1) Article 2 of the Treaty on European Union (TEU) states that the Union is founded on the values of respect for human dignity, equality, the rule of law and respect for human rights pursuant to the EU Charter of Fundamental Rights. According to Article 3(3) TEU, the Union shall work for the sustainable development of Europe and a high level of protection and improvement of the quality of the environment. Article 21 TEU states that the Union's action on the international scene shall be guided by the principles which have inspired its own creation, including the universality and indivisibility of human rights and respects for the principles of the United Nations Charter and international law. The Union shall define and pursue common policies and actions in order to, in particular, foster the sustainable economic, social and environmental development of developing countries.

(2) Delivering a European "Green Deal" and promoting European core values are among the priorities of the Union. These objectives require the involvement not only of the public authorities but also of private actors, in particular companies.

(3) In its Communication on A Strong Social Europe for Just Transition[71], the Commission committed to upgrading Europe's social market economy to achieve a just transition to

---

70 OJ C […], […], p. […].

71 Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions – A Strong Social Europe for Just Transitions (COM/2020/14 final).

sustainability. This Directive will also contribute to the European Pillar of Social Rights as both promote rights such as fair working conditions. It forms part of the EU policies and strategies relating to the promotion of decent work worldwide, including in global supply chains, as referred to in the Commission Communication on decent work worldwide[72].

(4) The behaviour of companies across all sectors of the economy is key to success in the EU's sustainability objectives as EU companies, especially large ones, rely on global value chains. It is also in the interest of companies to protect human rights and the environment, in particular given the rising concern of consumers and investors regarding these topics. Several initiatives fostering enterprises which support value-oriented transformation already exist on European[73], as well as national[74] level.

(5) Existing international standards on responsible business conduct specify the duty for companies to protect human rights and how they should address the protection of the environment across their operations and value chains. The United Nations Guiding Principles on Business and Human Rights[75] introduced the expectation that businesses exercise human rights due diligence, which expects that businesses identify, prevent and mitigate their adverse impacts and to account for how they address them. The Guiding Principles state that businesses should avoid infringing the human rights of others and should address adverse human rights impacts with which they are involved in their own operations and through their direct and indirect business relationships.

(6) This concept of due diligence for human rights was specified and further developed in the OECD Guidelines for Multinational Enterprises[76] which extended the application of due diligence to cover environmental and governance topics. The OECD Guidance on Responsible Business Conduct and sectoral guidance[77] are authoritative frameworks setting out practical due diligence steps and key characteristics to help companies identify, prevent, mitigate and account for how they address actual and potential impacts in their operations, supply chains and other business relationships. The concept of due diligence is also embedded in the recommendations of the ILO Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy.[78]

---

72 Communication from the Commission to the European Parliament, the Council and the European Economic and Social Committee on decent work worldwide for a global just transition and a sustainable recovery (COM(2022)66).

73 'Enterprise Models and the EU agenda', *CEPS Policy Insights*, No PI2021-02/ January 2021.

74 E.g. https://www.economie.gouv.fr/entreprises/societe-mission

75 United Nations' "Guiding Principles on Business and Human Rights: Implementing the United Nations 'Protect, Respect and Remedy' Framework", 2011.

76 OECD Guidelines for Multinational Enterprises, 2011 updated edition

77 OECD Guidance on Responsible Business Conduct, 2018, and sector-specific guidance.

78 The International Labour Organisation's "Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy, Fifth Edition, 2017, available at: https://www.ilo.org/empent/Publications/WCMS_094386/lang--en/index.htm.

(7) The United Nations' Sustainable Development Goals[79], adopted by all United Nations Member States in 2015, include the objectives to promote sustained, inclusive and sustainable economic growth. The Union has set itself the objective to deliver on the UN Sustainable Development Goals. The private sector contributes to these aims.

(8) International agreements under the United Nations Framework Convention on Climate Change, to which the EU and its Member States are parties, such as the Paris Agreement[80] and the recent Glasgow Climate Pact[81], set out precise avenues to address climate change and keep global warming within 1.5 C degrees. Besides specific actions being expected from all signatory Parties, the role of the private sector, in particular in its investment strategies, is considered central to achieve these objectives.

(9) In the European Climate Law[82], the Union also legally committed to becoming climate-neutral by 2050 and to reducing emissions by at least 55% by 2030. Both these commitments require changing the way in which companies produce and procure. The Commission's 2020 Climate Target Plan models various degrees of emission reductions required from different economic sectors, though all need to see considerable reductions under all scenarios for the EU to meet its climate objectives. The Plan also underlines that "changes in corporate governance rules and practices, including on sustainable finance, will make company owners and managers prioritise sustainability objectives in their actions and strategies." The 2019 Communication on the European Green Deal[83] sets out that all EU actions and policies should pull together to help the EU achieve a successful and just transition towards a sustainable future. It also sets out that sustainability should be further embedded into the corporate governance framework.

(10) Consistency with the Commission Communication on forging a climate-resilient Europe, presenting the EU Strategy on Adaptation to climate change, which specifically mentions that "any new investment and policy decision should be climate-informed and future-proof", including for "larger businesses managing supply chains"[84] is part of sustainable corporate due diligence. Similarly, there should be consistency with the Commission

---

79 https://www.un.org/ga/search/view_doc.asp?symbol=A/RES/70/1&Lang=E

80 https://unfccc.int/files/essential_background/convention/application/pdf/english_paris_agreement.pdf.

81 Glasgow Climate Pact, adopted on 13 November 2021 at COP26 in Glasgow, https://unfccc.int/sites/default/files/resource/cma2021_L16_adv.pdf.https://unfccc.int/sites/default/files/resource/cma2021_L16_adv.pdf.

82 Regulation (EU) 2021/1119 of the European Parliament and of the Council of 30 June 2021 establishing the framework for achieving climate neutrality and amending Regulations (EC) No 401/2009 and (EU) 2018/1999 ('European Climate Law') PE/27/2021/REV/1 (OJ L 243, 9.7.2021, p. 1–17).

83 https://ec.europa.eu/info/publications/communication-european-green-deal_en.https://ec.europa.eu/info/publications/communication-european-green-deal_en.

84 Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions on Forging a climate-resilient Europe – the new EU Strategy on Adaptation to Climate Change (COM/2021/82 final).

proposal for Capital Requirements Directive[85], which sets out clear requirements for banks' governance rules which includes ESG knowledge on boards (fit and proper/suitability tests); that ESG risks are covered in planning and that specific plans and targets for dealing with these are in place.

(11) This initiative can and should be consistent with the integration of the EU's sustainable development objectives as laid down in Articles 11 and 191 TFEU through the Commission's renewed objectives in Free Trade Agreements chapters on trade and sustainable development, which include climate change.

(12) An initiative on sustainable corporate governance was listed among the deliverables of the Action Plan on a Circular Economy[86], the Biodiversity strategy[87], the Farm to Fork strategy[88] and the Chemicals strategy[89] and Updating the 2020 New Industrial Strategy: Building a stronger Single Market for Europe's recovery[90], Industry 5.0[91] and the European Pillar of Social Rights Action Plan[92].

(13) The EU Action Plan on Human Rights and Democracy 2020-2024[93] sets as a priority to strengthen the EU's engagement to actively promote the global implementation of the United Nations Guiding Principles on Business and Human Rights and other relevant international guidelines such as the OECD Guidelines for Multinational Enterprises, including by advancing relevant due diligence standards.

(14) The European Parliament and the Council are calling on the Commission to propose legislation in the field of due diligence. In its resolution of 10 March 2021 with recommendations to the Commission on corporate due diligence and corporate

---

85 Proposal for a Directive of the European Parliament and the Council amending Directive 2013/36/EU as regards supervisory powers, sanctions, third-country branches, and environmental, social and governance risks, and amending Directive 2014/59/EU (COM/2021/663 final).

86 Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions on A new Circular Economy Action Plan For a cleaner and more competitive Europe (COM/2020/98 final).

87 Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions on the EU Biodiversity Strategy for 2030 Bringing nature back into our lives (COM/2020/380 final).

88 Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions on A Farm to Fork Strategy for a fair, healthy and environmentally-friendly food system (COM/2020/381 final).

89 Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions on the Chemicals Strategy for Sustainability Towards a Toxic-Free Environment (COM/2020/667 final).

90 Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions on Updating the 2020 New Industrial Strategy: Building a stronger Single Market for Europe's recovery (COM/2021/350 final)

91 Industry 5.0; https://ec.europa.eu/info/research-and-innovation/research-area/industrial-research-and-innovation/industry-50_en

92 https://op.europa.eu/webpub/empl/european-pillar-of-social-rights/en/

93 https://www.consilium.europa.eu/media/46838/st12848-en20.pdf

accountability, the European Parliament calls upon the Commission to propose EU rules for a comprehensive corporate due diligence obligation[94]. The Council Conclusions on Human Rights and Decent Work in Global Supply Chains of 1 December 2020 called upon the Commission to table a proposal for an EU legal framework on sustainable corporate governance, including cross-sector corporate due diligence obligations along global supply chains.[95] The European Parliament also calls for clarifying directors duties in its own initiative report adopted on 2 December 2020 on sustainable corporate governance. In their Joint Declaration on EU Legislative Priorities for 2022[96], the European Parliament, the Council of the European Union and the European Commission have committed, to deliver on an economy that works for people, to improve the regulatory framework on sustainable corporate governance.

(15) This Directive aims to ensure that companies active in the EU single market contribute to sustainable development and the sustainability transition of economies and societies through the prevention and mitigation of potential or actual adverse human rights and environmental impacts connected with companies' production processes and with respect to their products and services.

(16) Companies should take appropriate steps to set up and carry out due diligence measures, with respect to their own operations, their subsidiaries, as well as their established direct and indirect business relationships throughout their value chains in accordance with the provisions of this Directive, through what is referred to as an 'obligation of means'. This means that this Directive does not require companies to guarantee stopping adverse impacts in all circumstances. For example with respect to business relationships where the adverse impact results from State intervention, the company may not have the means to arrive at such results. The company should therefore take the appropriate measures which can reasonably be expected to result in prevention or minimisation of the adverse impact under the circumstances of the specific case, taking into account the specificities of its value chain, sector or geographical area in which they operate, and its power to influence its business relationships, both direct and indirect, and whether the company could increase such power.

(17) The due diligence process should encompass the six steps defined by the OECD Due Diligence Guidance for Responsible Business Conduct, which provides an authoritative framework aligned with the UN Guiding Principles on business and human rights (UNGPs) and OECD Guidelines for Multinational Enterprises, and covering due diligence measures for companies to identify and address adverse human rights and environmental impacts. This encompasses the following steps (1) integrating due diligence into policies and management systems, (2) identifying and assessing adverse human rights and

---

94 European Parliament resolution of 10 March 2021 with recommendations to the Commission on corporate due diligence and corporate accountability (2020/2129(INL)), P9_TA(2021)0073, available at https://oeil.secure.europarl.europa.eu/oeil/popups/ficheprocedure.do?lang=en&reference=2020/2129(INL).

95 Council Conclusions on Human Rights and Decent Work in Global Supply Chains, 1 December 2020 (13512/20)

96 Joint declaration of the European Parliament, the Council of the European Union and the European Commission on EU Legislative Priorities for 2022, available at https://ec.europa.eu/info/sites/default/files/joint_declaration_2022.pdf.

environmental impacts, (3) preventing, ceasing or minimising actual and potential adverse human rights, and environmental impacts, (4) assessing the effectiveness , (5) communicating, (6) providing for or cooperating in remediation.

(18) Adverse human rights and environmental impact occur in companies' own operations, subsidiaries, products, and in their value chains, in particular at the level of raw material sourcing, manufacturing, or at the level of product or waste disposal. In order for the due diligence to have a meaningful impact, it should cover human rights and environmental adverse impacts generated throughout the life-cycle of production and use and disposal of product or provision of services, at the level of own operations, subsidiaries and in value chains.

(19) The value chain should cover activities related to the production of a good or provision of services by a company, including the development of the product or the service and the use and disposal of the product as well as the related activities of established business relationships of the company. It should encompass upstream established direct and indirect business relationships that design, extract, manufacture, transport, store and supply raw material, products, parts of products, or provide services to the company that are necessary to carry out the company's activities, and also downstream relationships, including established direct and indirect business relationships, that use or receive products, parts of products or services from the company up to the end of life of the product, including inter alia the distribution of the product to retailers, the transport and storage of the product, dismantling of the product, its recycling, composting or landfilling.

(20) As regards financial sector undertakings providing loan, credit, securities underwriting or any other form of financing, insurance or reinsurance coverage, "value chain" with respect to the provision of such services should be limited to the activities of the clients receiving such loan, credit, other forms of financing insurance and reinsurance, and the subsidiaries thereof. The clients that are households and natural persons not acting in their capacity as business entrepreneurs, as well as small and medium sized undertakings should not be considered to be part of the value chain. The activities of the companies or other legal entities that are included in the value chain of that client should not be covered. This is also in line with relevant authoritative international frameworks as well as with recent sustainability-related EU law and legislative proposals in this area.

(21) In order to allow companies to properly identify the risks in their value chain and to make it possible for them to have leverage on their contractors and the subcontractors of those contractors, the due diligence obligations should be limited in this Directive to established business relationships. For the purpose of this Directive, established business relationships should mean such direct and indirect business relationships which are, or which are expected to be lasting, in view of their intensity and duration and which do not represent a negligible and ancillary part of the value chain. The relationships that would fall under this definition should be reassessed periodically, and at least every 12 months. If the direct business relationship of a company is labelled as established, then all its business relationships should also be considered as established regarding that company.

(22) Under this directive, EU companies with more than 500 employees on average and a worldwide net turnover exceeding EUR 150 million in the financial year preceding the last financial year should be required to comply with due diligence. As regards companies

which do not fulfil those criteria, but which had more than 250 employees on average and more than EUR 40 million worldwide net turnover in the financial year preceding the last financial year but not exceeding EUR 150 million net turnover nor 500 employees and which operate in one or more high-impact sectors, due diligence should apply 3 years after the end of the transposition period of this directive, in order to provide for a longer adaptation period. In order to ensure a proportionate burden, companies operating in such high-impact sectors should be required to comply with more targeted due diligence focusing on severe adverse impacts only and do a scoping exercise which is proportionate to their sector, value chains or the geographical regions in which they operate. Temporary agency workers, including those posted under Article 1(3), point (c), of Directive 96/71/EC of the European Parliament and of the Council[97], should be included in the calculation of the number of employees in the user company. Posted workers under Article 1(3), points (a) and (b), of Directive 96/71/EC should only be included in the calculation of the number of employees of the sending company.

(23) In order to reflect the priority areas of international action aimed at tackling human rights and environmental issues, the selection of high-impact sectors for the purposes of this Directive should be based on existing sectoral OECD due diligence guidance. The following sectors should be regarded as high-impact for the purposes of this Directive: the manufacture of textiles, leather and related products (including footwear), and the wholesale trade of textiles, clothing and footwear; agriculture, forestry, fisheries (including aquaculture), the manufacture of food products, and the wholesale trade of agricultural raw materials, live animals, wood, food, and beverages; the extraction of mineral resources regardless from where they are extracted (including crude petroleum, natural gas, coal, lignite, metals and metal ores, as well as all other, non-metallic minerals and quarry products), the manufacture of basic metal products, other non-metallic mineral products and fabricated metal products (except machinery and equipment), and the wholesale trade of mineral resources, basic and intermediate mineral products (including metals and metal ores, construction materials, fuels, chemicals and other intermediate products. As regards the financial sector, due to its specificities, even if it is covered by sector-specific OECD guidance, it should not form part of the high-impact sectors covered by this Directive. At the same time, in this sector, the broader coverage of actual and potential adverse impacts should be ensured by also including very large companies in the scope that do not have a legal form with limited liability, for instance cooperative credit institutions and insurance companies).

(24) In order to achieve fully the objectives of this Directive third-country companies with significant operations in the EU should also be covered. More specifically, the Directive should apply to third-country companies which generated a net turnover of at least EUR 150 million in the Union in the financial year preceding the last financial year or a net turnover of more than EUR 40 million but less than EUR 150 million in the financial year preceding the last financial year in one or more of the high-impact sectors, as of 3 years after the entry end of transposition period of this Directive.

---

97 Directive 96/71/EC of the European Parliament and of the Council of 16 December 1996 concerning the posting of workers in the framework of the provision of services (OJ L 18, 21.1.1997, p. 1).

(25) For defining the scope of application in relation to non-EU companies the described turnover criterion should be chosen as it creates a territorial connection between the third-country companies and the EU territory. Turnover is a proxy of the effects that the activities of these companies may have on the EU internal market. In accordance with the jurisprudence of the Court[98], such link is required for EU law to apply to third-country companies. To ensure identification of the relevant turnover of companies concerned, the methods for calculating net turnover for non-EU companies as laid down in Directive 2013/34/EU as amended by Directive (EU) 2021/2101 should be used. To ensure effective enforcement of this Directive, an employee threshold should, in turn, not be applied to determine which third-country companies fall under this Directive, as the notion of "employees" retained for the purposes of this Directive is based in Union law and cannot be properly applied outside of the Union. In the absence of a common methodology to determine the employees of third-country companies, such employee threshold would therefore create legal uncertainty and would be difficult to apply for supervisory authorities.

(26) In order to achieve a meaningful contribution to the sustainability transition, due diligence under this Directive should be carried out with respect to adverse human rights impact on protected persons resulting from the violation of one of the rights as enshrined in the international conventions as listed in the Annex to this Directive. Due diligence should further encompass adverse environmental impacts resulting from the violation of one of the prohibitions and obligations pursuant to the international environmental conventions listed in the Annex to this Directive.

(27) The United Nations Guiding Principles on Business and Human Rights recognise that companies can have an impact, directly or indirectly, on virtually the entire spectrum of internationally recognised human rights. In order to provide clarity to companies and give a reasonable dimension to the due diligence process, this Directive should define as precisely as possible the internationally recognized human rights in its scope. Internationally recognised human rights cover at a minimum the human rights contained in the Universal Declaration of Human Rights, as codified in the International Covenant on Civil and Political Rights and the International Covenant on Economic, Social and Cultural Rights and the principles concerning the fundamental rights in the ILO's Declaration on Fundamental Principles and Rights at Work and included in the ILO cores conventions, namely freedom of association and effective recognition of the right to collective bargaining; elimination of all forms of forced or compulsory labour; effective abolition of child labour; elimination of discrimination in respect of employment and occupation. Depending on circumstances, in the process of conducting human rights due diligence, companies may need to consider additional standards. They should pay special attention to any particular human rights impacts on individuals from groups or populations that may be at heightened risk of vulnerability or marginalisation, and bear in mind the different risks that may be faced by women and men.[99] In this connection, additional human rights instruments on the rights of women, indigenous peoples, national or ethnic, religious and

---

98 Principle from the Lotus Case, PCIJ, 1927.

99 Human rights due diligence, point 18 commentary, 2011 United Nations Guiding Principles on Business and Human Rights; https://www.ohchr.org/documents/publications/guidingprinciplesbusinesshr_en.pdf.

linguistic minorities, children, persons with disabilities are relevant. The eradication of labour exploitation forms the subject matter of United Nations Convention against transnational organized crime and the protocols thereto and the Palermo Protocol to Prevent, Suppress and Punish Trafficking in Persons Especially Women and Children, supplementing the United Nations Convention against Transnational Organized Crime.

(28) Moreover, companies in the scope of this Directive are obliged to comply with applicable EU climate, environmental and human rights legislation, including in particular the EU acquis with respect to climate and the environment and the EU Charter of Fundamental Rights.

(29) The Annex specifying the adverse human rights and environmental impacts takes into account that companies may have adverse impact on human rights in different ways. For example, the prohibition to deprive persons of life arbitrarily or unlawfully, which is enshrined in Article 3 of the Universal Declaration of Human Rights, may be violated through operations that pose life-threatening safety risks to workers or local populations through, for example, exposure to toxic chemicals or through the lethal use of force by security forces protecting company resources, facilities and personnel. The prohibition to impair the rights to liberty and security of the person in accordance with Article 9 of the International Covenant on Civil and Political Rights includes unlawful and arbitrary detention, threatening workers with physical punishment or tolerating severe harassment of some employees, allowing sexual abuse of female workers to go un-addressed in their workplace.

(30) Companies have guidance at their disposal that illustrates how their activities may impact human rights and which corporate behaviour is prohibited in accordance with internationally recognised human rights. Such guidance is included for instance in the United Nations Guiding Principles Reporting Framework[100] and the United Nations Guiding Principles Interpretative Guide[101]. Using relevant international guidelines and standards as a reference, the Commission should issue additional guidance that will serve as a practical tool for companies when carrying out human rights due diligence.

(31) In order to conduct appropriate human rights, and environmental due diligence with respect to their operations, their subsidiaries, and their value chains, companies covered by this Directive should integrate due diligence into corporate policies, identify, , prevent and minimise as well as bring to an end and minimize the extent of potential and actual adverse human rights and environmental impacts, establish and maintain a complaints procedure, monitor the effectiveness of the taken measures in accordance with the requirements that are set up in this Directive and communicate publicly on their due diligence.

(32) In order to ensure that due diligence forms part of companies' corporate policies, and in line with the relevant international framework, companies should integrate due diligence into all their corporate policies and have in place a due diligence policy. The due diligence

---

100 https://www.ungpreporting.org/wp-content/uploads/UNGPReportingFramework_withguidance2017.pdf

101 https://www.ohchr.org/Documents/Issues/Business/RtRInterpretativeGuide.pdf.https://www.ohchr.org/Documents/Issues/Business/RtRInterpretativeGuide.pdf.

policy should contain a description of the company's approach, including in the long term, to due diligence, a code of conduct describing the rules and principles to be followed by the company's employees and subsidiaries; a description of the processes put in place to implement due diligence, including the measures taken to verify compliance with the code of conduct and to extend its application to established business relationships. The code of conduct should apply in all relevant corporate functions and operations, including procurement and purchasing decisions. Companies should also update and publish their due diligence policy annually.

(33) To comply with due diligence, companies need to take appropriate measures to cease and prevent adverse impacts. An 'appropriate measure' should mean a measure that is capable of achieving the objectives of due diligence, commensurate with the degree of severity and the likelihood of the adverse impact, and reasonably available to the company, taking into account the circumstances of the specific case, including characteristics of the economic sector and of the specific business relationship and the company's influence thereof, and the need to ensure prioritisation of action. In this context, in line with international frameworks, the company's influence over a business relationship includes, on the one hand its ability to persuade the business relationship to take action to cease or prevent adverse impacts (for example through ownership or factual control, market power, pre-qualification requirements, linking business incentives to human rights and environmental performance, etc.) and, on the other hand, the degree of influence or leverage that the company could reasonably exercise, for example through cooperation with the business partner in question or engagement with another company which is the direct business partner of the business relationship associated with adverse impact.

(34) Under the due diligence obligations set out by this Directive, a company should identify actual or potential adverse human rights and environmental impacts. In order to allow for a comprehensive identification of adverse impacts, such identification should be based on quantitative and qualitative information. Identification should take into account impacts related to the sector, geography and to the company specifically. For instance, as regards adverse environmental impacts, the company should obtain information about baseline conditions at higher risk sites or facilities in value chains. Identification of adverse impacts should include assessing the human rights, and environmental context in a dynamic way and in regular intervals: prior to a new activity or relationship, prior to major decisions or changes in the operation (e.g. market entry, product launch, policy change, or wider changes to the business); in response to or anticipation of changes in the operating environment (e.g. rising social tensions); and periodically, at least every 12 months, throughout the life of an activity or relationship. Financial sector undertakings providing loan, credit, securities underwriting or any other form of financing, insurance or reinsurance coverage should identify the adverse impacts only at the inception of the contract. When identifying adverse impacts, companies should also identify and assess the impact of a business relationship's business model and strategies, including trading, procurement and pricing practices. When potential and actual adverse impacts are identified, they should be assessed based on their severity and likelihood. Where the company cannot prevent, cease or minimize all its adverse impacts at the same time, it should be able to prioritize its action, provided it takes the measures reasonably available to the company, taking into account the specific circumstances.

(35) In order to avoid undue burden on the smaller companies operating in high-impact sectors which are covered by this Directive, those companies should only be obliged to identify and assess those actual or potential adverse impacts that are particularly salient to the respective sector.

(36) In line with international standards, prevention and mitigation as well as bringing to an end and minimisation of adverse impacts should take into account the interests of those adversely impacted. For example, terminating a business relationship in which child labour was found may expose the child to even more severe adverse human rights impacts. This should therefore be taken into account when deciding on the appropriate action to take. For instance, contributions to ending the child labour found should include adjusting pricing practices to ensure a decent living of families and farmers, supporting to build schools and require the supplier to avoid child labour. In order to enable continuous engagement with the value chain business relationship instead of termination of business relation (disengagement) and possibly exacerbating adverse impacts, disengagement should be a last-resort action in line with the zero-tolerance on child labour policy of the European Union.

(37) Under the due diligence obligations set out by this Directive, if a company identifies potential adverse human rights or environmental impacts, it should take appropriate measures to prevent and minimise those. To provide companies with legal clarity and certainty, this Directive should define which actions companies should be required to take for prevention and minimisation of potential adverse impacts, while specifying the concrete situation in which the possible measures are relevant.

(38) So as to comply with the prevention and mitigation obligation under this Directive, companies should be required to take the following actions: where necessary due to the complexity of prevention measures, companies should develop and implement a prevention action plan. Companies should obtain contractual assurances from a direct partner with whom they have an established business relationship that it will ensure compliance with the code of conduct or the prevention action plan, including by seeking corresponding contractual assurances from its partners to the extent that their activities are part of the companies' value chain. The contractual assurances must be accompanied by the appropriate measures to verify compliance. To ensure comprehensive prevention of actual and potential adverse impacts, companies should also make investments which aim to prevent adverse impacts, provide targeted and proportionate support for an SME with which they have an established business relationships such as financing, for example, through direct financing, low-interest loans, guarantees of continued sourcing, and assistance in securing financing, to help implement the code of conduct or prevention action plan, or technical guidance such as in the form of training, management systems upgrading, and collaborate with other companies.

(39) In order to reflect the full range of options for the company in cases where potential impacts could not be addressed by the described prevention or minimisation measures, this Directive should also refer to the possibility for the company to seek to conclude a contract with the indirect relationship, with a view to achieving compliance with the company's code of conduct or a prevention action plan, and conduct appropriate measures to verify compliance of the indirect business relationship with the contract. This measure should be

taken with the agreement, or at least after information and consultation, of the intermediate contractors.

(40) In order to ensure that prevention and mitigation of potential adverse impacts is effective, companies should prioritize engagement with business relationships in the value chain, instead of terminating the business relationship, as a last resort action after attempting at preventing and mitigating adverse potential impacts without success. However, the Directive should also, for cases where potential adverse impacts could not be addressed by the described prevention or minimisation measures, refer to the obligation for companies to refrain from entering into new or extending existing relations with the partner in question and, where the law governing their relations so entitles them to, to either temporarily suspend commercial relationships with the partner in question, while pursuing prevention and minimisation efforts, if there is reasonable expectation that these efforts will succeed in the short-term; or to terminate the business relationship with respect to the activities concerned if the potential adverse impact is severe. In order to allow companies to fulfil that obligation, Member States should provide for the availability of an option to terminate the business relationship in contracts governed by their laws. It is possible that prevention of adverse impacts at the level of indirect business relationships requires collaboration with another company, for example a company which has a direct contractual relationship with the supplier. In some instances, such collaboration may be the only realistic way of preventing adverse impacts, in particular, where the indirect business relationship is not ready to enter into a contract with the company. In these instances, the company should collaborate with the entity which can most effectively prevent or minimize adverse impacts at the level of the indirect business relationship while respecting competition law.

(41) As regards direct and indirect business relationships, industry cooperation, industry schemes and multi-stakeholder initiatives can help create additional leverage to identify, mitigate, and prevent adverse impacts. Therefore it should be possible for companies to rely on such initiatives to support the implementation of their due diligence obligations laid down in this Directive to the extent that such schemes and initiatives are appropriate to support the fulfilment of those obligations. Companies may assess, at their own initiative, the alignment of these schemes and initiatives with the obligations under this Directive and according to internationally recognised guidance. In order to ensure full information on such initiatives, the Directive should also refer to the possibility for the Commission and the Member States to facilitate the dissemination of information on such schemes or initiatives and their outcomes. The Commission, in collaboration with Member States, may issue guidance for assessing the fitness of industry schemes and multi-stakeholder initiatives.

(42) Under the due diligence obligations set out by this Directive, if a company identifies actual human rights or environmental adverse impacts, it should take appropriate measures to bring those to an end. It can be expected that a company is able to bring to an end actual adverse impact in their own operations. However, it should be clarified that, as regards established business relationships, where adverse impacts cannot be brought to an end, companies should minimise the extent of such impacts. To provide companies with legal clarity and certainty, this Directive should define which actions companies should be required to take for bringing actual human rights and environmental adverse impacts to an

end and mitigation of their extent while specifying the concrete situation in which the possible measures are relevant.

(43) So as to comply with the obligation of bringing to an end and minimising the extent of actual adverse impacts under this Directive, companies should be required to take the following actions: neutralise the adverse impact or minimise its extent, with an action proportionate to the significance and scale of the adverse impact and to the contribution of the company's conduct to the damage. Where necessary due to the fact that the adverse impact cannot be immediately brought to an end, companies should develop and implement a corrective action plan with reasonable and clearly defined timelines for action and qualitative and quantitative indicators for measuring improvement. Companies should also seek contractual assurances from a direct business partner with whom they have an established business relationship that they will ensure compliance with the company's code of conduct and, as necessary, a prevention action plan, including by seeking corresponding contractual assurances from its partners, to the extent that their activities are part of the company's value chain The contractual assurances should be accompanied by the appropriate measures to verify compliance. Finally, companies should also make investments aiming at ceasing or minimising the extent of adverse impact, and collaborate with other entities, including, where relevant, to increase the company's ability to cease the adverse impact.

(44) In order to reflect the full range of options for the company in cases where actual impacts could not be addressed by the described measures, this Directive should also refer to the possibility for the company to seek to conclude a contract with the indirect relationship, with a view to achieving compliance with the company's code of conduct or a prevention action plan, and conduct appropriate measures to verify compliance of the indirect business relationship with the contract. This measure should be taken with the agreement, or at least after information and consultation, of the intermediate contractors.

(45) In order to ensure that bringing actual adverse impacts to an end or minimising them is effective, companies should prioritize engagement with business relationships in the value chain, instead of terminating the business relationship, as a last resort action after attempting at bringing actual adverse impacts to an end or minimising them without success. However, the Directive should also, for cases where actual adverse impacts could not be brought to an end or adequately mitigated by the described measures, refer to the obligation for companies to refrain from entering into new or extending existing relations with the partner in question and, where the law governing their relations so entitles them to, to either temporarily suspend commercial relationships with the partner in question, while pursuing efforts to bring to an end or minimise the adverse impact, or terminate the business relationship with respect to the activities concerned, if the adverse impact is considered severe. In order to allow companies to fulfil that obligation, Member States should provide for the availability of an option to terminate the business relationship in contracts governed by their laws.

(46) In order to make possible for affected or potentially affected persons and organisations, to raise grievances, companies should provide the possibility for such persons and organisations to submit complaints directly to them in case of legitimate concerns regarding actual or potential human rights and environmental adverse impacts. Organisations who

may submit such complaints should include trade unions and other workers' representatives representing individuals working in the value chain concerned and civil society organisations active in the areas related to the value chain concerned where they have knowledge about a potential or actual adverse impact. Companies should establish a procedure for dealing with those complaints and inform workers, trade unions and other workers' representatives, where relevant, about such processes. Recourse to the complaints and remediation mechanism should not prevent the complainant from having recourse to judicial remedies. In accordance with international standards, complaints should be entitled to request from the company appropriate follow-up on the complaint and to meet with the company's representatives at an appropriate level to discuss potential or actual severe adverse impacts that are the subject matter of the complaint. This access should not lead to unreasonable solicitations of companies.

(47) Companies should monitor the implementation and effectiveness of their due diligence policy and the measures they have taken to prevent, mitigate, cease or minimise potential or actual adverse impacts in accordance with the due diligence obligation, for example, by carrying out periodic assessments of their own activities, their subsidiaries and their business relationships. Such assessments should verify that adverse impacts are properly identified, due diligence measures are implemented and adverse impacts have actually been prevented or ceased. In order to ensure that such assessments are up-to-date, they should be carried out at least every 12 months and be revised in-between if there are reasonable grounds to believe that significant new risks of adverse impact may have arisen.

(48) In accordance with existing international standards set by the United Nations Guiding Principles on Business and Human Rights and the OECD framework, it forms part of the due diligence requirement to communicate externally relevant information on due diligence policies, processes and activities conducted to identify and address actual or potential adverse impacts, including the findings and outcomes of those activities. The proposal for the Directive on Corporate Sustainability Reporting sets out relevant reporting obligations for the companies covered by this directive. In order to avoid duplicating reporting obligations, this Directive should therefore not introduce any new reporting obligations in addition to those under Directive 2013/34/EU as amended by the Directive on Corporate Sustainability Reporting for the companies covered by that Directive as well as the reporting standards that will be developed under it. As regards companies that are within the scope of this Directive, but do not fall under Directive 2013/34/EU, in order to comply with their obligation of communicating as part of the due diligence under this Directive, they should publish on their website an annual statement in a language customary in the sphere of international business.

(49) In order to ensure uniform conditions for the implementation of this communication obligation for companies not falling under Directive 2013/34/EU, implementing powers should be conferred on the Commission. Those powers should be exercised in accordance

with Regulation (EU) No 182/2011 of the European Parliament and of the Council[102]. The examination procedure should be used for the adoption of those implementing acts.

(50) In order to facilitate companies' cascading of their due diligence requirements through their value chain, the Commission should provide guidance on model contractual clauses.

(51) In order to provide support to companies and Member State authorities on how companies can fulfil their due diligence obligations, the Commission, in consultation with the European Union Agency for Fundamental Rights, the European Environment Agency and the Executive Agency for Small and Medium-sized Enterprises and relevant international bodies having expertise with due diligence implementation, should have the possibility to issue guidelines, where necessary.

(52) Although SMEs are not included in the scope of this Directive, they will be impacted by its provisions as contractors or subcontractors to the companies which are in the scope. The aim is nevertheless to mitigate financial or administrative burden on SMEs, which are already struggling in the context of the global economic and sanitary crisis. In order to support SMEs to implement due diligence, Member States should set up and operate, either individually or jointly, dedicated websites, portals or platforms, and Member States may financially support SMEs and help them build capacity. Such support should also be made accessible, and where necessary adapted and extended to upstream economic operators in third countries. Companies whose business partner is an SME, are also encouraged to support them in fulfilling the due diligence requirements as a consequence of the cascading, in case such requirements would jeopardize the viability of the SME and use fair, reasonable, non-discriminatory and proportionate requirements to the SME resources and capacity.

(53) In order to complement Member State support to SMEs, the Commission will build on existing EU tools, projects and other actions helping with the due diligence implementation in the EU and in third countries. It may set up new support measures that provide help to companies, including SMEs on due diligence requirements, including an observatory for value chain transparency and the facilitation of joint stakeholder initiatives.

(54) The Commission and Member States will continue to work in partnership with third countries to support upstream economic operators build the capacity to effectively prevent and mitigate adverse human rights and environmental impacts of their operations and business relationships, paying specific attention to the challenges faced by smallholders. They will use their neighbourhood, development and international cooperation instruments to support third country governments and upstream economic operators in third countries addressing adverse human rights and environmental impacts of their operations and upstream business relationships. This may include working with partner country governments, the local private sector and stakeholders on addressing the root causes of adverse human rights and environmental impacts.

---

[102] Regulation (EU) No 182/2011 of the European Parliament and of the Council of 16 February 2011 laying down the rules and general principles concerning mechanisms for control by Member States of the Commission's exercise of implementing powers (OJ L 55, 28.2.2011, p. 13).

(55) In order to allow for the effective oversight of and, where necessary, enforcement of this Directive in relation to those companies that are not governed by the law of a Member State, these companies should designate a sufficiently mandated authorised representative in the Union and provide information relating to their authorised representatives. It should be possible for the authorised representative to also function as point of contact, provided the relevant requirements of this Directive are complied with.

(56) In order to ensure the monitoring of the correct implementation of companies' due diligence obligations and ensure the proper enforcement of this Directive, Member States should designate one or more national supervisory authorities. These supervisory authorities should be of a public nature, independent from economic actors, and free of conflicts of interest. In accordance with national law, Member States should ensure appropriate financing of the competent authority. They should be entitled to carry out investigations, on their own initiative or based on complaints or substantiated concerns raised under this Directive. In addition to the supervision, Member States could also use various instruments e.g. access to state support, public procurement, to incentivise companies to comply with their due diligence obligations.

(57) In order to ensure effective enforcement of national measures implementing this Directive, Member States should provide for dissuasive, proportionate and effective sanctions for infringements of those measures. In order for such sanction regime to be effective, administrative sanctions to be imposed by the national supervisory authorities should include pecuniary sanctions. Where the legal system of a Member State does not provide for administrative sanctions as foreseen in this Directive, the rules on administrative sanctions may be applied in such a way that the sanction is initiated by the competent supervisory authority and imposed by the judicial authority. Therefore, it is necessary that those Member States ensure that the application of the rules and sanctions has an equivalent effect to the administrative sanctions imposed by the competent supervisory authorities. When imposing such sanctions, the judicial authority should take into account the recommendation by the competent supervisory authority initiating the sanction.

(58) In order to ensure consistent application and enforcement of national provisions adopted pursuant to this Directive, national supervisory authorities should cooperate and coordinate their action. For that purpose a European Network of Supervisory Authorities should be set up by the Commission and the supervisory authorities should assist each other in performing their tasks and provide mutual assistance.

(59) In order to ensure effective enforcement of the obligations laid down in this Directive, including as regards compensation of victims of adverse impacts for damages, Member States should be required to lay down rules in line with the provisions of this Directive, governing the civil liability of the company for damages arising due to its failure to comply with the due diligence process. The company should be liable for damages if they failed to comply with the obligations to prevent and minimise potential adverse impacts or to bring actual impacts to an end and mitigate their extent, and as a result of this failure an adverse impact that should have been identified, prevented, minimised, ceased or mitigated through the appropriate measures occurred and led to damage.

(60) As regards damages occurring at the level of established indirect business relationships, the liability of the company should be subject to specific conditions. The company should

only be liable if it did not comply with some of the due diligence measures. However, the company should not be exonerated from liability through implementing such measures in case it was unreasonable to expect that the action actually taken, including as regards verifying compliance, would be adequate to prevent, minimise, cease or mitigate the adverse impact. For example, even if the company, through contractual cascading, has requested half-yearly reporting from the business partner about its action to eliminate forced labour, such control measure, due to the severe nature of the human rights abuse, should not in itself be considered reasonably adequate to prevent forced labour if there is evidence of its systematic character and if no additional verification steps regarding its elimination by that business partner are taken. The liability regime does not regulate who should prove that the company's action was reasonably adequate under the circumstances of the case, therefore this question is left to national law.

(61) As regards civil liability rules, the civil liability of a company for damages arising due to its failure to carry out adequate due diligence should be without prejudice to civil liability of its subsidiaries or the respective civil liability of direct and indirect business partners in the value chain. Also, the civil liability rules under this Directive should be without prejudice to stricter civil liability rules related to adverse environmental impacts or to adverse human rights impacts provided for in other EU or national legislation.

(62) As regards civil liability arising from adverse environmental impacts, persons who suffer damage to their property, health, safety etc. can claim compensation for such damages under this Directive even where they overlap with human rights claims. Furthermore, the competent court can also require compliance and remedial action by ordering the cessation of infringements and, where appropriate, to impose remedies proportionate to the infringement and necessary to bring the infringement effectively to an end, as well as through interim measures.

(63) In order to ensure that victims of human rights and environmental harms can bring an action for damages and claim compensation for damages arising due to a company's failure to comply with the due diligence obligations stemming from this Directive, even where the law applicable to such claims is not the law of a Member State, as could be for instance be the case in accordance with international private law rules when the damage occurs in a third country, this Directive should require Member States ensure that the liability under this Directive not denied in such cases. For instance, this protection should target natural persons for human rights, and should allow natural persons and companies and other legal persons who, for example, own or rent the land where the environmental damage occurred to ask for damages.

(64) The civil liability regime under this Directive should be without prejudice to the Environmental Liability Directive 2004/35/EC. This Directive should not prevent Member States from imposing further, more stringent obligations on companies or from otherwise taking further measures having the same objectives as that Directive.

(65) In all Member States' national laws, directors owe a duty of care to the company. In order to ensure that this general duty is understood and applied in a manner which is coherent and consistent with the due diligence obligations introduced by this Directive, this Directive should clarify, in a harmonised manner, the general duty of care of directors to act in the best interest of the company, by laying down that directors take into account the

human rights and environmental consequences, including in the long term, of their decisions. Directors should also identify other risks to the company's operations and related to sustainability matters as referred to in Directive 2013/34/EU as amended by the Corporate Sustainability Reporting Directive, including, where applicable, climate change. Furthermore, directors should adopt a plan to ensure that the business model and strategy of the company are compatible with the transition to a sustainable economy and with the limiting of global warming to 1.5 °C in line with the Paris Agreement. In case climate change is identified as a principal risk for the company's operations, the plan should include indicative emission reduction objectives. Finally, directors should ensure that such plan is duly taken into account in directors' remuneration to contribute to the company's business strategy and long-term interests and sustainability, and that clear, comprehensive and varied criteria are established for the award of any variable remuneration.

(66) Responsibility for due diligence should be assigned to the company's directors, in line with the international due diligence frameworks. Directors should therefore be responsible for putting in place and overseeing the due diligence actions as laid down in this Directive and for adopting the company's due diligence policy, taking into account the input of stakeholders and civil society organisations and integrating due diligence into corporate management systems. Directors should also adapt the corporate strategy to actual and potential impacts identified and any due diligence measures taken.

(67) Persons who work for companies subject to due diligence obligations under this Directive or who are in contact with such companies in the context of their work-related activities can play a key role in exposing breaches of the rules of this Directive. They can thus contribute to preventing and deterring such breaches and strengthening the enforcement of this Directive. Directive (EU) 2019/1937 of the European Parliament and of the Council[103] should therefore apply to the reporting of all breaches of this Directive and to the protection of persons reporting such breaches.

(68) This Directive should be applied in compliance with Union data protection law and the right to the protection of privacy and personal data as enshrined in Articles 7 and 8 of the Charter of Fundamental Rights of the European Union. Any processing of personal data under this Directive is to be undertaken in accordance with Regulation (EU) 2016/679 of the European Parliament and of the Council[104], including the requirements of purpose limitation, data minimisation and storage limitation.

---

103 Directive (EU) 2019/1937 of the European Parliament and of the Council of 23 October 2019 on the protection of persons who report breaches of Union law (OJ L 305, 26.11.2019, p. 17).

104 Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC (General Data Protection Regulation) OJ L 119, 4.5.2016, p. 1–88.

(69) The European Data Protection Supervisor was consulted in accordance with Article 28(2) of Regulation (EU) 2018/1725 of the European Parliament and of the Council[105] and delivered an opinion on … 2022.

(70) This Directive is without prejudice to the application of more stringent or more specific requirements in EU social, environmental, home affairs[106], financial services or other internal market legislation, and in any sector-specific Union legislative act regulating specific types of companies, entities, service providers, products, production processes, or any specific subject-matter with the same objectives as this Directive. Those specific provisions should be considered *lex specialis* in relation to this Directive and should take precedence over this Directive to the extent that they are more specific, or more stringent, and have the same objective, nature and effect as the provisions of this Directive. The specific provisions of such Union legislative act should not be interpreted in a way that undermines the effective application of this Directive or the achievement of its general aim nor any aspects that are not regulated in the specific Union legislative act (e.g. civil liability). The mere existence of specific Union provisions in a particular sector or field, in particular other EU legislative instruments that lay down requirements regarding value chain due diligence, should not exclude the application of this Directive. Where this Directive provides for more specific provisions or adds requirements to the provisions laid down in other Union legislative act including those on due diligence, the provisions laid down by those Union legislative acts should apply in conjunction with those of this Directive.

(71) In order to ensure consistency between this Directive and Regulation (EU) 2020/852 of the European Parliament and of the Council[107], this Directive should take appropriate account of the minimum safeguards established by the Regulation, ensuring a consistent approach with the procedures implemented to that purpose.

(72) Since the objective of this Directive, namely contributing to sustainable development through the prevention and mitigation of potential or actual human rights and environmental adverse impacts in companies' value chains, cannot be sufficiently achieved by the Member States, but can rather, by reason of the scale and effects of the actions, be better achieved at Union level, the Union may adopt measures, in accordance with the principle of subsidiarity as set out in Article 5 TEU. In accordance with the principle of proportionality, as set out in that Article, this Directive does not go beyond what is necessary in order to achieve that objective.

---

105 Regulation (EU) 2018/1725 of the European Parliament and of the Council of 23 October 2018 on the protection of natural persons with regard to the processing of personal data by the Union institutions, bodies, offices and agencies and on the free movement of such data (OJ L 295, 21.11.2018, p. 39).

106 Directive (EU) 2011/36 of the European Parliament and of the Council of 5 April 2011 on preventing and combating trafficking in human beings and protecting its victims, and replacing Council Framework Decision 2002/629/JHA (OJ L 101, 15.4.2011).

107 Regulation (EU) 2020/852 of the European Parliament and of the Council of 18 June 2020 on the establishment of a framework to facilitate sustainable investment, and amending Regulation (EU) 2019/2088 (OJ L 198, 22.6.2020, p. 13–43).

HAVE ADOPTED THIS DIRECTIVE:

Article 1

Subject matter

1. This Directive lays down rules

   (a) on obligations for companies regarding actual and potential human rights and environmental adverse impacts, with respect to their own operations, the operations of their subsidiaries, and the value chain operations carried out by entities with whom the company has an established business relationship and

   (b) on liability for violations of the obligations mentioned above.

   The nature of business relationships as 'established' shall be reassessed periodically, and at least every 12 months.

2. This Directive shall not constitute grounds for reducing the level of protection of human rights or of protection of the environment provided by the law of Member States at the time of the adoption of this Directive.

Article 2

Scope

1. This Directive shall apply to companies which are formed in accordance with the legislation of a Member State and which fulfil one of the following conditions:

   (a) the company had more than 500 employees on average and had a net turnover of more than EUR 150 million in the last financial year for which annual financial statements have been prepared;

   (b) the company did not reach the thresholds under point (a), but had more than 250 employees on average and had a net turnover of more than EUR 40 million in the last financial year for which annual financial statements have been prepared, provided that at least 50% of this net turnover was generated in one or more of the following sectors:

      (i) the manufacture of textiles, leather and related products (including footwear), and the wholesale trade of textiles, clothing and footwear;

      (ii) agriculture, forestry, fisheries (including aquaculture), the manufacture of food products, and the wholesale trade of agricultural raw materials, live animals, wood, food, and beverages;

      (iii) the extraction of mineral resources regardless from where they are extracted (including crude petroleum, natural gas, coal, lignite, metals and metal ores, as well as all other, non-metallic minerals and quarry products), the manufacture of basic metal products, other non-metallic mineral products and fabricated metal products (except machinery and equipment), and the

wholesale trade of mineral resources, basic and intermediate mineral products (including metals and metal ores, construction materials, fuels, chemicals and other intermediate products).

2. This Directive shall also apply to companies which are formed in accordance with the legislation of a third country and fulfil one of the following conditions:

   (a) generated a net turnover of more than EUR 150 million in the Union in the financial year preceding the last financial year;

   (b) generated a net turnover of more than EUR 40 million but not more than EUR 150 million in the Union in the financial year preceding the last financial year, provided that at least 50% of its net worldwide turnover was generated in one or more of the sectors listed in paragraph 1, point (b).

3. For the purposes of paragraph 1, the number of part-time employees shall be calculated on a full-time equivalent basis. Temporary agency workers shall be included in the calculation of the number of employees in the same way as if they were workers employed directly for the same period of time by the company.

4. As regards the companies referred to in paragraph 1, the Member State competent to regulate matters covered in this Directive shall be the Member State in which the company has its registered office.

Article 3

Definitions

For the purpose of this Directive, the following definitions shall apply:

(a) 'company' means any of the following:

   (i) a legal person constituted as one of the legal forms listed in Annex I to Directive 2013/34/EU of the European Parliament and of the Council[108],

   (ii) a legal person constituted in accordance with the law of a third country in a form comparable to those listed in Annex I and II of that Directive,

   (iii) a legal person constituted as one of legal forms listed in Annex II to Directive 2013/34/EU composed entirely of undertakings organised in one of the legal forms falling within points (i) and (ii);

   (iv) a legal person, regardless of its legal form, which is

[108] Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings (OJ L 182, 29.6.2013, p. 19)

– an insurance undertaking within the meaning of Article 2(1) of Council Directive 91/674/EEC[109], or

– a financial sector entity as defined in Article 4, point 27, of Regulation (EU) No 575/2013 of the European Parliament and of the Council[110];

(b) 'adverse environmental impact' means an adverse impact on the environment resulting from the violation of one of the prohibitions and obligations pursuant to the international environmental conventions listed in the Annex, Part II;

(c) 'adverse human rights impact' means an adverse impact on protected persons resulting from the violation of one of the rights or prohibitions listed in the Annex Part I A, as enshrined in the international conventions listed in the Annex, Part I B;

(d) 'subsidiary' means a 'controlled undertaking' as defined in Article 2(1), point (f), of Directive 2004/109/EC of the European Parliament and of the Council[111];

(e) 'business relationship' means a relationship with a contractor, subcontractor or any other legal entities ('partner')

(i) with whom the company has a commercial agreement or to whom the company provides financing , insurance or reinsurance, or

(ii) that performs business operations related to the products or services of the company for, or on behalf of the company;

(f) 'established business relationship' means a business relationship, whether direct or indirect, which is, or which is expected to be lasting, in view of its intensity or duration and which does not represent a negligible or merely ancillary part of the value chain.

(g) 'value chain' means activities related to the production of a good or provision of services by a company, including the development of the product or the service and the use and disposal of the product as well as the related activities of upstream and downstream established business relationships of the company. As regards companies within the meaning of point (a)(iv), 'value chain' with respect to the provision of these specific services shall include the activities of the clients receiving such loan, credit, other forms of financing, insurance or reinsurance. The value chain of such financial sector undertakings shall also cover the subsidiaries of such clients that are linked to activities for which the contract is concluded. The value chain of such financial sector does not cover SMEs receiving loan, credit, financing , insurance or reinsurance of such entities;

---

109 Council Directive 91/674/EEC of 19 December 1991 on the annual accounts of insurance undertakings (OJ L 374, 31.12.1991, p. 7).

110 Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (OJ L 176, 27.6.2013, p. 1).

111 Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC (OJ L 390, 31.12.2004, p. 38).

(h) ‘independent third-party verification’ means verification of the compliance by a company, or parts of its value chain, with human rights and environmental requirements resulting from the provisions of this Directive by an auditor which is independent from the company, free from any conflicts of interests, has experience and competence in environmental and human rights matters and is accountable for the quality and reliability of the audit;

(i) ‘SME’ means a micro, small or a medium-sized enterprise, irrespective of its legal form, that is not part of a large group, as those terms are defined in Article 3(1), (2), (3) and (7) of Directive 2013/34/EU;

(j) ‘industry initiative’ means a combination of voluntary value chain due diligence procedures, tools and mechanisms, including independent third-party verifications, developed and overseen by governments, industry associations or groupings of interested organisations;

(k) ‘authorised representative’ means a natural or legal person resident or established in the Union who has a mandate from a company within the meaning of point (a)(ii) to act on its behalf in relation to compliance with that company’s obligations pursuant to this Directive;

(l) ‘severe adverse impact’ means an adverse environmental impact or an adverse human rights impact that is especially significant by its nature, or affects a large number of persons or a large area of the environment, or which is irreversible, or particularly difficult to remedy as a result of the measures necessary to restore the situation prevailing prior to the impact;

(m) ‘net turnover’ means

(i) the ‘net turnover’ as defined in Article 2, point (5), of Directive 2013/34/EU; or,

(ii) where the company applies international accounting standards adopted on the basis of Regulation (EC) No 1606/2002 of the European Parliament and of the Council[112] or is a company within the meaning of point (a)(ii), the revenue as defined by or within the meaning of the financial reporting framework on the basis of which the financial statements of the company are prepared;

(n) ‘stakeholders’ means the company’s employees, the employees of its subsidiaries, and other individuals, groups, communities or entities whose rights or interests are or could be affected by the products, services and operations of that company, its subsidiaries and its business relationships;

(o) ‘director’ means:

(i) any member of the administrative, management or supervisory bodies of a company;

---

[112] Regulation (EC) No 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards (OJ L 243, 11.9.2002, p.1).

(ii) where they are not members of the administrative, management or supervisory bodies of a company, the chief executive officer and, if such function exists in a company, the deputy chief executive officer;

(iii) other persons who perform functions similar to those performed under point (i) or (ii);

(p) 'board of directors' means the administrative or supervisory body responsible for supervising the executive management of the company, or, if no such body exists, the person or persons performing equivalent functions;

(q) 'appropriate measure' means a measure that is capable of achieving the objectives of due diligence, commensurate with the degree of severity and the likelihood of the adverse impact, and reasonably available to the company, taking into account the circumstances of the specific case, including characteristics of the economic sector and of the specific business relationship and the company's influence thereof, and the need to ensure prioritisation of action.

Article 4

Due diligence

1. Member States shall ensure that companies conduct human rights and environmental due diligence as laid down in Articles 5 to 11 ('due diligence') by carrying out the following actions:

(a) integrating due diligence into their policies in accordance with Article 5;

(b) identifying actual or potential adverse impacts in accordance with Article 6;

(c) preventing and minimising potential adverse impacts, and bringing actual adverse impacts to an end and mitigating their extent in accordance with Articles 7 and 8;

(d) establishing and maintaining a complaints procedure in accordance with Article 9;

(e) monitoring the effectiveness of their due diligence policy and measures in accordance with Article 10;

(f) publicly communicating on due diligence in accordance with Article 11.

2. Member States shall ensure that, for the purposes of due diligence, companies are entitled to share resources and information within their respective groups of companies and with other legal entities in compliance with applicable competition law.

Article 5

Integrating due diligence into companies' policies

1. Member States shall ensure that companies integrate due diligence into all their corporate policies and have in place a due diligence policy. The due diligence policy shall contain all of the following:

(a) a description of the company's approach, including in the long term, to due diligence;

(b) a code of conduct describing rules and principles to be followed by the company's employees and subsidiaries;

(c) a description of the processes put in place to implement due diligence, including the measures taken to verify compliance with the code of conduct and to extend its application to established business relationships.

2. Member States shall ensure that the companies update and publish their due diligence policy annually.

Article 6

Identifying actual and potential adverse impacts

1. Member States shall ensure that companies take appropriate measures to identify actual and potential adverse human rights impacts and adverse environmental impacts arising from their own operations or those of their subsidiaries and, where related to their value chains, from their established business relationships, in accordance with paragraph 2, 3 and 4.

2. By way of derogation from paragraph 1, companies referred to in Article 2(1), point (b), and Article 2(2), point (b), shall only be required to identify actual and potential adverse severe impacts relevant to the respective sector mentioned in Article 2(2), point (b)(i)-(iii).

3. When companies referred to in Article 3, point (a)(iv), provide credit, loan or financing pursuant to [CRD/CRR] or insurance and reinsurance in accordance with [Solvency II], identification of actual and potential adverse human rights impacts and adverse environmental impacts shall be carried out only before providing that service and in respect of the entity to whom that service is being provided. The value chain of such financial sector undertakings shall also cover the subsidiaries of such clients that are linked to activities for which the contract is concluded.

4. Member States shall ensure that, for the purposes of identifying the adverse impacts referred to in paragraph 1, companies are entitled to make use of appropriate resources, including independent reports and information gathered through the complaints procedure provided for in Article 9. Companies shall, where relevant, also carry out consultations with potentially affected groups including workers and other relevant stakeholders to gather information on actual or potential adverse impacts.

Article 7

Preventing and minimising of potential adverse impacts

1. Member States shall ensure that companies take appropriate measures to prevent, or where prevention is not possible or not immediately possible, minimise potential adverse human rights impacts and adverse environmental impacts that have been, or should have been, identified pursuant to Article 6, in accordance with paragraphs 2, 3 4 and 5 of this Article.

2. Companies shall be required to take the following actions, where relevant:

(a) where necessary due to the nature or complexity of the measures required for prevention, develop and implement a prevention action plan, with reasonable and clearly defined timelines for action and qualitative and quantitative indicators for measuring improvement. Where relevant, the prevention action plan shall be developed in consultation with stakeholders;

(b) seek contractual assurances from a business partner with whom it has a direct business relationship that it will ensure compliance with the company's code of conduct and, as necessary, a prevention action plan, including by seeking corresponding contractual assurances from its partners, to the extent that their activities are part of the company's value chain (contractual cascading). When such contractual assurances are obtained, paragraph 4 shall apply;

(c) make necessary investments, such as into management or production processes and infrastructures, to comply with paragraph 1;

(d) provide targeted and proportionate support for an SME with which the company has an established business relationship, where compliance with the code of conduct or the prevention action plan would jeopardise the viability of the SME.

3. As regards potential adverse impacts that could not be prevented or adequately minimised by the measures in paragraph 2, the company may seek to conclude a contract with a partner with whom it has an indirect relationship, with a view to achieving compliance with the company's code of conduct or a prevention action plan. When such a contract is concluded, paragraph 4 shall apply.

4. When contractual assurances are obtained from, or a contract is entered into with an SME, the terms shall be fair, reasonable and non-discriminatory. The contractual assurances or the contract shall be accompanied by the appropriate measures to verify compliance. For the purposes of verifying compliance, the company may refer to suitable industry initiatives or independent third-party verification. Where such checks are carried out, the company should bear the cost of the independent third-party verification;

5. As regards potential adverse impacts within the meaning of paragraph 1 that could not be prevented or adequately minimised by the measures in paragraphs 2, 3 and 4, the company shall be required to refrain from entering into new or extending existing relations with the partner in connection with or in the value chain of which the impact has arisen and shall, where the law governing their relations so entitles them to, take the following actions:

(g) temporarily suspend commercial relations with the partner in question, while pursuing prevention and minimisation efforts, if there is reasonable expectation that these efforts will succeed in the short-term;

(h) terminate the business relationship with respect to the activities concerned if the potential adverse impact is severe.

Member States shall provide for the availability of an option to terminate the business relationship in contracts governed by their laws.

Article 8

Bringing actual adverse impacts to an end and mitigating their extent

1. Member States shall ensure that companies take appropriate measures to bring actual adverse impacts that have been, or should have been, identified pursuant to Article 6 to an end, in accordance with paragraphs 2 to 6 of this Article.

2. Where the adverse impact cannot be brought to an end, Member States shall ensure that companies minimise the extent of such an impact.

3. Companies shall be required to take the following actions, where relevant:

   (a) neutralise the adverse impact or minimise its extent, including by the payment of damages to the affected persons and of financial compensation to the affected communities. The action shall be proportionate to the significance and scale of the adverse impact and to the contribution of the company's conduct to the adverse impact;

   (b) where necessary due to the fact that the adverse impact cannot be immediately brought to an end, develop and implement a corrective action plan with reasonable and clearly defined timelines for action and qualitative and quantitative indicators for measuring improvement. Where relevant, the corrective action plan shall be developed in consultation with stakeholders;

   (c) obtain contractual assurances from a direct partner with whom it has an established business relationship that it will ensure compliance with the code of conduct and, as necessary, a corrective action plan, including by seeking corresponding contractual assurances from its partners, to the extent that they are part of the value chain (contractual cascading). When such contractual assurances are obtained, paragraph 5 shall apply.

   (d) make necessary investments, such as into management or production processes and infrastructures to comply with paragraphs 1, 2 and 3;

   (e) provide targeted and proportionate support for an SME with which the company has an established business relationship, where compliance with the code of conduct or the corrective action plan would jeopardise the viability of the SME;

   (f) in compliance with Union law including competition law, collaborate with other entities, including, where relevant, to increase the company's ability to bring the adverse impact to an end, in particular where no other action is suitable or effective.

4. As regards actual adverse impacts that could not be brought to an end or adequately mitigated by the measures in paragraph 3, the company may seek to conclude a contract with a partner with whom it has an indirect relationship, with a view to achieving compliance with the company's code of conduct or a corrective action plan. When such a contract is concluded, paragraph 5 shall apply.

5. When contractual assurances are obtained from, or a contract is entered into, with an SME, the terms used shall be fair, reasonable and non-discriminatory. The contractual assurances or the contract shall be accompanied by the appropriate measures to verify compliance. For the purposes of verifying compliance, the company may refer to suitable

industry initiatives or independent third-party verification. Where such checks are carried out, the company should bear the cost of the independent third-party verification.

6. As regards actual adverse impacts within the meaning of paragraph 1 that could not be brought to an end or adequately mitigated by the measures provided for in paragraphs 3 4 and 5, the company shall refrain from entering into new or extending existing relations with the partner in connection to or in the value chain of which the impact has arisen and shall, where the law governing their relations so entitles them to, take one of the following actions:

   (a) temporarily suspend commercial relationships with the partner in question, while pursuing efforts to bring to an end or minimise the adverse impact, or

   (b) terminate the business relationship with respect to the activities concerned, if the adverse impact is considered severe.

   Member States shall provide for the availability of an option to terminate the business relationship in contracts governed by their laws.

Article 9

Complaints procedure

1. Member States shall ensure that companies provide the possibility for persons and organisations listed in paragraph 2 to submit complaints to them where they have legitimate concerns regarding actual or potential adverse human rights impacts and adverse environmental impacts with respect to their own operations, the operations of their subsidiaries and their value chains.

2. Member States shall ensure that the complaints may be submitted by:

   (a) persons who are affected or have reasonable grounds to believe that they might be affected by an adverse impact,

   (b) trade unions and other workers' representatives representing individuals working in the value chain concerned,

   (c) civil society organisations active in the areas related to the value chain concerned.

1. Member States shall ensure that the companies establish a procedure for dealing with complaints referred to in paragraph 1, including a procedure when the company considers the complaint to be unfounded, and inform the relevant workers and trade unions of those procedures. Member States shall ensure that where the complaint is well-founded, the adverse impact that is the subject matter of the complaint is deemed to be identified within the meaning of Article 6.

2. Member States shall ensure that complaints are entitled

   (a) to request appropriate follow-up on the complaint from the company with which they have filed a complaint pursuant to paragraph 1, and

(b) to meet with the company's representatives at an appropriate level to discuss potential or actual severe adverse impacts that are the subject matter of the complaint.

Article 10

Monitoring

Member States shall ensure that companies carry out periodic assessments of their own operations and measures, those of their subsidiaries and, where related to the value chains of the company, those of their established business relationships, to monitor the effectiveness of the identification, prevention, minimisation, bringing to an end and mitigation of human rights and environmental adverse impacts. Such assessments shall be based, where appropriate, on qualitative and quantitative indicators and be carried out at least every 12 months and whenever there are reasonable grounds to believe that significant new risks of the occurrence of those adverse impacts may arise. The due diligence policy shall be updated in accordance with the outcome of those assessments.

Article 11

Communicating

Member States shall ensure that companies that are not subject to reporting requirements under Articles 19a and 29a of Directive 2013/34/EU publish on their website an annual statement in a language customary in the sphere of international business. The statement shall be published by 30 April each year, covering the previous calendar year.

The Commission shall adopt an implementing act laying down the criteria for such reporting, such as a description of due diligence, potential and actual adverse impacts and actions taken on those. Those implementing acts shall be adopted in accordance with the examination procedure referred to in Article 27(2).

Article 12

Model contractual clauses

In order to provide support to companies to facilitate their compliance with Article 7(2), point (b), and Article 8(3), point (c), the Commission shall adopt guidance about voluntary model contract clauses.

Article 13

Guidelines

In order to provide support to companies or to Member State authorities on how companies should fulfil their due diligence obligations, the Commission, in consultation with the European Union Agency for Fundamental Rights, the European Environment Agency, the European Innovation Council and Small and Medium-sized Enterprises Executive Agency, and where appropriate with international bodies having expertise in due diligence, may issue guidelines, for specific sectors or specific adverse impacts, where necessary.

Article 14

Accompanying measures

1. Member States shall, in order to provide information and support to companies and the partners with whom they have established business relationships in their value chains in their efforts to fulfil the obligations resulting from this Directive, set up and operate individually or jointly dedicated websites, platforms or portals. Specific consideration shall be given, in that respect, to the SMEs that are present in the value chains of companies.

2. Without prejudice to applicable State aid rules, Member States may financially support SMEs.

3. The Commission may complement Member States' support measures building on existing Union action to support due diligence in the Union and in third countries and devising new measures, including facilitation of joint stakeholder initiatives to help companies fulfil their obligations.

4. Companies may rely on industry schemes and multi-stakeholder initiatives to support the implementation of their obligations referred to in Articles 5 to 11 of this Directive to the extent that such schemes and initiatives are appropriate to support the fulfilment of those obligations. The Commission and the Member States may facilitate the dissemination of information on such schemes or initiatives and their outcome. The Commission, in collaboration with Member States, may issue guidance for assessing the fitness of industry schemes and multi-stakeholder initiatives.

Article 15

Authorised representative

1. Member States shall ensure that each company referred to in Article 2(2) designates a legal or natural person as its authorised representative, established or domiciled in one of the Member States where it operates. The designation shall be valid when confirmed as accepted by the authorised representative.

2. Member States shall ensure that the name, address, electronic mail address and telephone number of the authorised representative is notified to a supervisory authority in the Member State where the authorised representative is domiciled or established. Member States shall ensure that the authorised representative is obliged to provide, upon request, a copy of the designation in an official language of a Member State to any of the supervisory authorities.

3. Member States shall ensure that a supervisory authority in the Member State where the authorised representative is domiciled or established and, where it is different, a supervisory authority in the Member State in which the company generated most of its net turnover in the Union in the financial year preceding the last financial year are informed that the company is a company within the meaning of Article 2(2).

4. Member States shall ensure that each company empowers its authorised representative to receive communications from supervisory authorities on all matters necessary for

compliance with and enforcement of national provisions transposing this Directive. Companies shall be required to provide their authorised representative with the necessary powers and resources to cooperate with supervisory authorities.

Article 16

Supervisory Authorities

1. Each Member State shall designate one or more supervisory authorities to supervise compliance with the obligations laid down in national provisions adopted pursuant to Articles 6 to 11 ('supervisory authority').

2. As regards the companies referred to in Article 2(1), the competent supervisory authority shall be that of the Member State in which the company has its registered office.

3. As regards companies referred to in Article 2(2), the competent supervisory authority shall be that of the Member State in which the company has a branch. If the company does not have a branch in any Member State, or has branches located in different Member States, the competent supervisory authority shall be the supervisory authority of the Member State in which the company generated most of its net turnover in the Union in the financial year preceding the last financial year before the date indicated in Article 29 or the date on which the company first fulfils the criteria laid down in Article 2(2), whichever comes last.

   Companies referred to in Article 2(2) may, on the basis of a change in circumstances leading to it generating most of its turnover in the Union in a different Member State, make a duly reasoned request to change the supervisory authority that is competent to regulate matters covered in this Directive in respect of that company.

4. Where a Member State designates more than one supervisory authority, it shall ensure that the respective competences of those authorities are clearly defined and that they cooperate closely and effectively with each other.

5. By the date indicated in Article 29 Member States shall inform the Commission of the names and contact details of the supervisory authorities designated pursuant to this Article, as well as of their respective competence where there are several designated supervisory authorities. They shall inform the Commission of any changes thereto.

6. The Commission shall make publicly available, including on its website, a list of the supervisory authorities. The Commission shall regularly update the list on the basis of the information received from the Member States.

7. Member States shall guarantee the independence of the supervisory authorities and shall ensure that they, and all persons working for or who have worked for them and auditors or experts acting on their behalf, exercise their powers impartially, transparently and with due respect for obligations of professional secrecy. In particular, Member States shall ensure that the authority is legally and functionally independent from the companies falling within the scope of this Directive or other market interests, that its staff and the persons responsible for its management are free of conflicts of interest, subject to confidentiality requirements, and that they refrain from any action incompatible with their duties.

Article 17

Powers of supervisory authorities

1. Member States shall ensure that the supervisory authorities have adequate powers and resources to carry out the tasks assigned to them under this Directive, including the power to request information and carry out investigations related to compliance with the obligations set out in this Directive.

2. A supervisory authority may initiate an investigation on its own motion or as a result of substantiated concerns communicated to it pursuant to Article 18, where it considers that it has sufficient information indicating a possible breach by a company of the obligations provided for in the national provisions adopted pursuant to this Directive.

   Inspections shall be conducted in compliance with the national law of the Member State in which the inspection is carried out and with prior warning to the company, except where prior notification hinders the effectiveness of the inspection. Where, as part of its investigation, a supervisory authority wishes to carry out an inspection on the territory of a Member State other than its own, it shall seek assistance from the supervisory authority in that Member State pursuant to Article 20(2).

3. If, as a result of the actions taken pursuant to paragraphs 1 and 2, a supervisory authority identifies a failure to comply with national provisions adopted pursuant to this Directive, it shall grant the company concerned an appropriate period of time to take remedial action, if such action is possible.

   Taking remedial action does not preclude the imposition of administrative sanctions or the triggering of civil liability in case of damages, in accordance with Articles 19 and 21, respectively.

4. When carrying out their tasks, supervisory authorities shall have at least the following powers:

   (a) to order the cessation of infringements of the national provisions adopted pursuant to this Directive, abstention from any repetition of the relevant conduct and, where appropriate, remedial action proportionate to the infringement and necessary to bring it to an end;

   (b) to impose pecuniary sanctions in accordance with Article 19;

   (c) to adopt interim measures to avoid the risk of severe and irreparable harm.

5. Where the legal system of the Member State does not provide for administrative sanctions, this Article and Article 19 may be applied in such a manner that the sanction is initiated by the competent supervisory authority and imposed by the competent national courts, while ensuring that those legal remedies are effective and have an equivalent effect to the administrative sanctions imposed by supervisory authorities.

6. Member States shall ensure that each natural or legal person has the right to an effective judicial remedy against a legally binding decision by a supervisory authority concerning them.

Article 18

Substantiated concerns

1. Member States shall ensure that natural and legal persons are entitled to submit substantiated concerns to any supervisory authority when they have reasons to believe, on the basis of objective circumstances, that a company is failing to comply with the national provisions adopted pursuant to this Directive ('substantiated concerns').

2. Where the substantiated concern falls under the competence of another supervisory authority, the authority receiving the concern shall transmit it to that authority.

3. Member States shall ensure that supervisory authorities assess the substantiated concerns and, where appropriate and necessary, exercise their powers as referred to in Article 17.

4. The supervisory authority shall, as soon as possible and in accordance with the relevant provisions of national law and in compliance with Union law, inform the person referred to in paragraph 1 of the result of the assessment of their substantiated concern and shall provide the reasoning for it.

5. Member States shall ensure that the persons submitting the substantiated concern according to this Article and having, in accordance with national law, a legitimate interest in the matter have access to a court or other independent and impartial public body competent to review the procedural and substantive legality of the decisions, acts or failure to act of the supervisory authority.

Article 19

Sanctions

6. Member States shall lay down the rules on sanctions applicable to infringements of national provisions adopted pursuant to this Directive, and shall take all measures necessary to ensure that they are implemented. The sanctions provided for shall be effective, proportionate and dissuasive.

7. In deciding whether to impose sanctions and, if so, in determining their nature and appropriate level, due account shall be taken of the company's efforts to comply with any remedial action required of them by a supervisory authority, any investments made and any targeted support provided pursuant to Articles 7 and 8, as well as collaboration with other entities to address adverse impacts in its value chains, as the case may be.

8. When pecuniary sanctions are imposed, they shall be based on the company's turnover.

9. Member states shall ensure that decision of the supervisory authorities containing sanctions related to the breach of the provisions of this directive should be published.

10. Member States shall notify to the Commission the provisions of their laws which they adopt pursuant to this Article [by OP please insert date = date of transposition of this amending Directive] and, without delay, any subsequent amendment law or amendment affecting them.

Article 20

European Network of Supervisory Authorities

1. The Commission shall set up a European Network of Supervisory Authorities, composed of representatives of the supervisory authorities. The Network shall facilitate the cooperation of the supervisory authorities and the coordination and alignment of regulatory, investigative, sanctioning and supervisory practices of the supervisory authorities and, as appropriate, sharing of information among them.

   The Commission may invite Union agencies with relevant expertise in the areas covered by this Directive to join the European Network of Supervisory Authorities.

2. Supervisory authorities shall provide each other with relevant information and mutual assistance in carrying out their duties and shall put in place measures for effective cooperation with each other. Mutual assistance shall include requests for information and collaboration with a view to the exercise of the powers referred to in Article 17, including in relation to inspections.

3. Supervisory authorities shall take all appropriate steps needed to reply to a request for assistance by another supervisory authority without undue delay and no later than 1 month after receiving the request. Such steps may include, in particular, the transmission of relevant information on the conduct of an investigation.

4. Requests for assistance shall contain all the necessary information, including the purpose of and reasons for the request. Supervisory authorities shall only use the information received through a request for assistance for the purpose for which it was requested.

5. The requested supervisory authority shall inform the requesting supervisory authority of the results or, as the case may be, of the progress regarding the measures to be taken in order to respond to the request for assistance.

6. Supervisory authorities shall not charge each other fees for actions and measures taken pursuant to a request for assistance.

   However, supervisory authorities may agree on rules to indemnify each other for specific expenditure arising from the provision of assistance in exceptional cases.

7. The supervisory authority that is competent pursuant to Article 16(3) shall inform the European Network of Supervisory Authorities of that fact and of any request to change the competent supervisory authority.

8. When doubts exist as to the attribution of competence, the information on which that attribution is based will be shared with the European Network of Supervisory Authorities, which may coordinate efforts to find a solution.

Article 21

Civil liability

1. Member States shall ensure that companies are liable for damages if:

   (a) they failed to comply with the obligations laid down in Articles 7 and 8 and;

(b) as a result of this failure an adverse impact that should have been identified, prevented, minimised, brought to an end or its extent mitigated through the appropriate measures laid down in Articles 7 and 8 occurred and led to damage.

2. Notwithstanding paragraph 1, Member States shall ensure that where a company has taken the actions referred to in Article 7 paragraph 2 point (b) and Article 8 paragraph 3 point (c), it shall not be liable for damages caused by an adverse impact arising as a result of the activities of an indirect partner with whom it has an established business relationship, unless it was unreasonable, in the circumstances of the case, to expect that the action actually taken, including as regards verifying compliance, would be adequate to prevent, minimise, bring to an end or mitigate the adverse impact.

In the assessment of the existence and extent of liability under this paragraph, due account shall be taken of the company's efforts, insofar as they relate directly to the damage in question, to comply with any remedial action required of them by a supervisory authority, any investments made and any targeted support provided pursuant to Articles 7 and 8, as well as any collaboration with other entities to address adverse impacts in its value chains.

3. The civil liability of a company for damages arising under this provision shall be without prejudice to the civil liability of its subsidiaries or of any direct and indirect business partners in the value chain.

4. The civil liability rules under this Directive shall be without prejudice to stricter civil liability rules related to adverse environmental impacts or to adverse human rights impacts provided for in other Union or national legislation.

5. Member States shall ensure that the liability provided for in paragraphs 1 to 3 of this Article is not denied on the sole ground that the law applicable to such claims is not the law of a Member State.

Article 22

Reporting of breaches and protection of reporting persons

Directive (EU) 2019/1937 shall apply to the reporting of all breaches of this Directive and the protection of persons reporting such breaches.

Article 23

Public procurement and public support

In accordance with Article 18(2) of Directive 2014/24/EU, Article 36(2) of Directive 2014/25/EU and Article 30(3) of Directive 2014/23/EU, Member States shall take appropriate measures to ensure that in the performance of public procurement or concession contracts companies comply with the obligations laid down in [national provisions adopted pursuant to] Articles 5, 6, 7, 8, 9, 10 and 11 of this Directive.

Member States shall ensure that companies applying for public support provide evidence that they have not been sanctioned for a failure to comply with the obligations of this Directive.

Article 24

Directors' duty of care

1. Member States shall ensure that, when fulfilling their duty to act in the best interest of the company, directors of companies referred to in Article 2(1) take into account the human rights, climate and environmental consequences, including in the long term, of their decisions.

2. Member States shall ensure that, in view of their general duty of care as referred to in this Article, directors identify other risks to the company's operations related to sustainability matters as referred to in [CSRD], including, where applicable, climate change.

3. Member States shall ensure that directors adopt a plan to ensure that the business model and strategy of the company are compatible with the transition to a sustainable economy and with the limiting of global warming to 1.5 ℃ in line with the Paris Agreement. In case climate change is identified as a principal risk for the company's operations, the plan shall include indicative emission reduction objectives.

4. Directors shall ensure that the plan referred to in paragraph 3, is duly taken into account in directors' remuneration to contribute to the company's business strategy and long-term interests and sustainability, and that clear, comprehensive and varied criteria are established for the award of any variable remuneration.

5. Member States shall ensure that their laws, regulations and administrative provisions providing for a breach of directors' duties apply also to the provisions of this Article.

Article 25

Setting up and overseeing due diligence

1. Member States shall ensure that directors of companies referred to in Article 2(1) are responsible for putting in place and overseeing the due diligence actions referred to in Article 4 and in particular the due diligence policy referred to in Article 5, with due consideration for relevant input from stakeholders and civil society organisations. The directors shall report to the board of directors in that respect.

2. Member States shall ensure that directors take steps to adapt the corporate strategy to take into account the actual and potential adverse impacts identified pursuant to Article 6 and any measures taken pursuant to Articles 7 to 9.

Article 26

Amendment to Directive (EU) No 2019/1937

In Point E.2 of Part I of the Annex to Directive (EU) No 2019/1937, the following point is added:

‘(vi) [Directive … of the European Parliament and of the Council of … on Corporate Sustainability Due Diligence and amending Directive (EU) 2019/1937*+]’

Article 27

Committee procedure

1. The Commission shall be assisted by a committee. That committee shall be a committee within the meaning of Regulation (EU) No 182/2011.

2. Where reference is made to this paragraph, Article 5 of Regulation (EU) No 182/2011 shall apply.

Article 28

Review

No later than … [*OP please insert the date = 7 years after the date of entry into force of this Directive]*, the Commission shall submit a report to the European Parliament and to the Council on the implementation of this Directive. The report shall evaluate the effectiveness of this Directive in reaching its objectives and assess the following issues:

(a) whether the thresholds regarding the number of employees and net turnover laid down in Article 2(1) need to be lowered;

(b) whether the list of sectors in Article 2(1), point (b), needs to be changed, including in order to align it to guidance from the Organisation for Economic Cooperation and Development.

Article 29

Transposition

1. Member States shall adopt and publish, by … [*OJ to insert: 2 years from the entry into force of this Directive]* at the latest, regulations and administrative provisions necessary to comply with this Directive. They shall forthwith communicate to the Commission the text of those provisions.

   They shall apply those provisions as follows:

   (a) from… [OJ to insert: 2 years from the entry into force of this Directive] as regards companies referred to in Article 2(1), point (a), and Article 2(2), point (a);

   (b) from … [OJ to insert: 5 years from the entry into force of this Directive] as regards companies referred to in Article 2(1), point (b), and Article 2(2), point (b).

+ OJ: Please insert in the text the number and the date of the Directive contained in document ... and insert the OJ reference of that Directive in the footnote.

When Member States adopt those provisions, they shall contain a reference to this Directive or be accompanied by such a reference on the occasion of their official publication. Member States shall determine how such reference is to be made.

2. Member States shall communicate to the Commission the text of the main provisions of national law which they adopt in the field covered by this Directive.

Article 30

Entry into force

This Directive shall enter into force on the twentieth day following that of its publication in the *Official Journal of the European Union*.

Article 31

Addressees

This Directive is addressed to the Member States.

Done at Brussels,

For the European Parliament	*For the Council*
The President	*The President*