

Strelia ESG Series

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The proposal for a directive on Corporate Sustainability Due Diligence is definitely making its way

On 1 June 2023, the European Parliament agreed its position on the Corporate Sustainability Due Diligence Directive (CSDDD). Soon, negotiations on the final text will start between the Parliament, the Council and the Commission with the objective of agreeing on the final text by probably early next year. The Directive will then have to be implemented into the national legislation within two following years and it will apply based on a phased-in approach.

The Directive imposes due diligence obligations and a liability regime with regards to human rights abuses and environmental harm in the targeted companies' global value chains. The companies will have to adopt a transition plan in line with the general objective to restrict global warming to 1,5°C as per the Paris Agreement.

Once transposed, the Directive will have a significant impact on numerous companies. The CSDDD allows for public and private enforcement regarding the companies' accountability for environmental and human rights impact in particular as regards potentially misleading climate neutrality statements, greenwashing and mismatch between declarations and the actual actions. As such, the CSDDD will likely open doors even wider to climate and human rights related litigation and class action claims and shareholder activism against the companies, financial institutions and corporate directors. This trend is clearly visible already in the several European countries, including the UK and the Netherlands, but also advancing in Belgium.

Extended scope, inclusion of financial services and application

In the Parliament's position, the scope of the CSDDD is significantly extended. It will apply to an increased number of EU and non-EU companies subject to specific quantitative criteria as regards the minimum number of employees and the minimum net worldwide turnover.

It will also apply to companies active in the financial sector.

The CSDDD will apply within three or four years from its entry into force, depending on the targeted companies' size.

Back to the value chain concept

In Parliament's position, and differently from the Council's view, the concept of value chain has been reinstated. Accordingly, both up-stream activities – relating largely to production – and down-stream activities – i.e., post-production activities – are targeted.

Fight against climate change and greenwashing

In the Parliament's view, the targeted companies will have to implement a transition plan in line with the reporting requirements of the Corporate Sustainability Reporting Directive. The goal is to ensure that the companies' business model and strategy are aligned with the transition to a sustainable economy and with the limiting of global warming to 1.5°C as per the Paris Agreement and the objective of achieving climate neutrality as established in the European Climate Law. The plan must be based on scientifically verified independent solutions.

This transition plan must include, among others, a description of specific targets related to climate change and emissions reduction and of the companies' progress as well as of the specific roles to be fulfilled in achieving the plan by the companies' corporate bodies, i.e. administration, management and supervisory bodies.

Prevention, ending and remediating adverse impact

The adverse impact of the companies' activities will have to be prevented or, where possible, ended, by a broad range of measures, e.g. by adapting specific business models and strategies, including purchasing practices, among which those that contribute to wages and income for their suppliers, and developing and using purchase policies that do not encourage potential or actual adverse impact on human rights or the environment. Institutional investors and asset managers will have to act e.g. by engaging with the investee company and by exercising voting rights in line with the Shareholder Rights Directive (SRD 2).

Where the adverse impact has already occurred, it will have to be remediated with the aim of restoring the affected persons and groups or communities and/or the environment to a situation equivalent or as close as possible to their situation before the impact. The companies' remedial measures may include compensation, restitution, rehabilitation, public apologies, reinstatement or a contribution to investigations.

Increased due diligence in troubled times

Companies operating in conflict or post-conflict areas, in occupied or annexed territories or in fragile areas with weak or non-existent governance and security must fulfill obligations following from international humanitarian law and increased due diligence on their operations. Specifically, they must integrate a thorough analysis of the conflict, its root causes, triggers and parties involved as well as of the impact of the companies' activities on the conflict.

Duty of care and variable remuneration of directors

If it were up to the Parliament, the companies' directors will be personally incentivized to make sure appropriate transition plans are in place and implemented. Large companies must notably adopt a remuneration policy to ensure that the variable remuneration for directors is linked to the company's climate change transition plan.

Extension of civil liability and possible sanctions

Another far-reaching element is the extension of the companies' civil liability in the event the companies fail to comply with the obligations in accordance with the CSDDD.

The safe harbour exclusion of civil liability for companies that seek contractual assurances from a business partner with whom they have a direct business relationship would be deleted. Moreover:

- the limitation period for bringing actions for damages is at least ten years,
- costs of the proceedings will not be prohibitively expensive for claimants to seek justice,
- claimants can seek injunctive measures, including summary proceedings, in the form of a definitive or provisional measure to cease an action which may be in breach of the CSDDD, or to comply with a measure under this regime,
- mandated trade unions, civil society organisations, or other relevant actors acting in the public interest can bring actions before a court on behalf of a victim or a group of victims,
- when a claimant has indicated that additional evidence lies in the control of the company, courts will be able to order that such evidence be disclosed by the company in accordance with national procedural law,
- upon request of a court, supervisory authorities will share any information they may have at their disposal about a given company with the court.

Also the national supervisory authorities will have specific extended powers, such as to impose pecuniary sanctions, issue public statements regarding the companies, issue cease and desist orders or suspend products from free circulation or export and exclusion.

Next steps

The draft CSDDD will now be discussed and further negotiated between the EU Parliament, the Council and the Commission. The likely difficult points will be the scope of application to financial services, the civil liability and the variable remuneration of the directors, as these elements are viewed differently by the three EU institutions. Stay tuned!



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