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COMMISSION STAFF WORKING DOCUMENT

Follow-up to the second opinion of the Regulatory Scrutiny Board

Accompanying the document

Proposal for a

DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL

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

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1. FINDINGS OF THE SECOND OPINION OF THE REGULATORY SCRUTINY BOARD

Following the negative opinion of the Regulatory Scrutiny Board (hereafter: the Board) on the first draft impact assessment report on the Sustainable Corporate Governance initiative of 7 May 2021, a revised impact assessment was submitted to the Board for a second opinion on 5 November 2021. While noting the significant revision responding to its initial comments, the Board nevertheless maintained its negative opinion on 26 November 2021[1], referring to the following main shortcomings:

1. *problem description* remaining vague and not providing convincing evidence that EU businesses, in particular small and medium-sized enterprises (SMEs), do not already sufficiently reflect sustainability aspects;
2. *policy options* remaining too limited, not identifying key policy choices;
3. *assessment of impacts* not being sufficiently complete, balanced and neutral, and uncertainty related to the realisation of benefits not being sufficiently reflected; and
4. *proportionality of the preferred option* not sufficiently demonstrated.

This document provides additional evidence and explanations in response to the above listed main findings and the specific suggestions for improvement provided by the Board (for a summary of how these were addressed, please refer to Annex 3). As such, this document **complements the impact assessment**[2], which was not revised in substance and is published in parallel together with the opinions of the Regulatory Scrutiny Board, thus allowing for transparency and comparability. This document also complements the information provided in the Explanatory Memorandum accompanying the proposal.

It is important to stress that the opinions of the Regulatory Scrutiny Board are an assessment of the quality of the impact assessment and not an assessment of the related legislative proposal. They further led to **adjustments of the preferred option** that had been put forward by the impact assessment. The corresponding changes made to the proposal, as presented for adoption, are also explained in this document.

2. THE PROBLEM AND ITS EVOLUTION

This section responds to the Board's recommendation to specify better the problem definition and present a more balanced dynamic baseline scenario that integrates better specific market and regulatory developments in the EU and in third countries (see Annex 3: Overview table, General comment 1 and Specific comments 1-2).

[1] SEC(2022)95.

[2] Commission Staff Working Document: "Impact Assessment Report Accompanying the document Proposal for a Directive of the European Parliament and the Council on Corporate Sustainability Due Diligence and amending Directive (EU) 2019/37" (SWD(2022)42.

4.1. Increasing uptake of sustainability practices and shortcomings

The impact assessment presents evidence that many companies are already improving the sustainability of their business operations. This is further supported by **new evidence** showing that more than 90% of CEOs state that **sustainability is important to their company's success** and **many companies develop sustainability strategies, and market sustainable products or services**.[3] The EcoVadis Business Sustainability Risk and Performance Index 2021, which is based on sustainability ratings, shows that the general sustainability performance of rated companies is increasing across regions and industries, and this trend can be expected to continue.[4] Europe is the leading region in that respect. For instance, the use of supplier codes of conduct and supplier assessments has grown in 2020 from 14% to 26% and from 24% to 33% of companies, respectively, compared to 2016.

However, **progress in some areas remains slow**. According to the EcoVadis index mentioned above, key actions such as supply chain risk analysis remain underutilised. As a result, **less than 35% of the surveyed companies have policies on sustainable procurement and supply chain due diligence in place**.

Moreover, according to the 2021 European Sustainable Industry Barometer, while most **industry federations** have embedded sustainability in general in their agendas, **fewer are directly undertaking relevant activities** (e.g. target setting, leading impact projects and providing annual disclosures).[5] **Significant disparities still exist among different industry sectors**.[6]

In light of increased calls for transparency in the value chain from investors and consumers, it is expected, on the one hand, that **corporate commitments on sustainability will further develop**.[7] On the other hand, as explained in the impact assessment, such pressure is **not sufficient to mainstream the mitigation of adverse**

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[3] Hoffman, A. J. (2018). The Next Phase of Business Sustainability. *Stanford Social Innovation Review*, *16*(2), 35–39.

[4] The EcoVadis Business Sustainability Risk and Performance Index 2021: Insights on global supply chains ratings covers the period 2016-2020 and is based on data derived over 72 000 ratings conducted on more than 46 000 companies.

[5] From the interviewed industry federations, only 40% have included SDGs explicitly in their mission and vision, 40% include time-bound targets in their sustainability roadmaps, 30% engage in practical sustainability impact/improvement projects with their members, and only 30% participated in EU-funded sustainability projects. See 2021 European Sustainable Industry Barometer – Assessing the maturity and integration of sustainability factors in European industry, a report based on research produced by CSR Europe and V.E, part of Moody's ESG Solutions, page 28 of the report.

[6] Industry federations from the materials sectors outperform those from consumer and retail-focused sectors (see page 12 of the same report).

[7] By way of example, in the lead up to COP 26, over 970 companies globally have reportedly set science-based targets. A 2021 survey by the Energy & Climate Intelligence Unit and Oxford Net Zero found that 21% of the 2 000 publicly listed companies surveyed had committed to net zero emissions by 2050 at the latest. However, the same survey also found that there was considerable variation in the quality of business commitments with regard to their scope, governance mechanisms and implementation plans. A recent benchmarking study by Climate Action 100+ found that of the 159 largest corporate emitters surveyed, no company performed at a high level across all 9 indicators including the presence of a decarbonisation strategy, capital allocation alignment, climate policy engagement and climate governance.

human rights and environmental impacts across all large companies. Furthermore, without mandatory action, investors and consumers would miss consistent benchmarks to be assured about the value chain standards, while companies would lack clarity about due diligence standard to implement in the value chain. Hence, **mandatory action would lower transactions costs** within the value chain and **create a level playing field**.

4.2. Links with other regulatory due diligence measures and with measures under the European Green Deal

This initiative **complements existing Union legislative measures and legislative proposals** that have already been adopted, or are being prepared, **that set out sectoral or product-specific due diligence requirements**. It also **contributes to the comprehensive package of measures under the Green Deal**. This section focuses on the evolution of the problem in light of those relevant measures, complementing section 2.3 of the impact assessment.

The product-related and sector-specific Union initiatives setting out due diligence obligations **aim at improving specific sustainability concerns** in supply or value chains of certain products and sectors and are **targeted at specific economic activities**. The **Conflict Minerals Regulation**[8] which covers gold, tin, tungsten and tantalum supply chains. The **Deforestation Proposal** (proposal for a Regulation on deforestation-free products)[9] concerns specific agricultural products, i.e. beef, palm oil, soy, wood, cocoa, coffee and derived products.[10] The **Batteries Proposal** (proposal for a Regulation concerning batteries and waste batteries)[11] establishes a supply chain due diligence requirement related to specific kinds of industrial electric-vehicle batteries.

The above-mentioned measures aim at **addressing very specific pressing sustainability concerns** that are particularly salient as regards the specific product concerned. The Conflict Minerals Regulation aims at cutting finance of armed groups and abolishing forced labour and other limited very serious human rights abuses, corruption and money laundering in relation to the trade of the products in question. The Deforestation proposal aims at addressing deforestation risk only. The Batteries Proposal addresses both environmental and human/labour rights concerns related to the battery in question.

In addition, the Communication on decent work worldwide[12] has announced that the Commission is preparing a new legislative proposal that will effectively prohibit the

[8] 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.
[9] 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.
[10] Further commodities can be added at a later stage.
[11] 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
[12] 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 final.

placing on the Union market of products made by forced labour, including forced child labour. The new initiative will cover both domestic and imported products and combine a ban with a robust, risk-based enforcement framework. The new instrument will build on international standards and complement horizontal and sectoral initiatives, in particular the due diligence obligations as laid down in this proposal.

The Corporate Sustainability Due Diligence initiative sets up a horizontal due diligence requirements that serve as a common denominator for companies in the scope that are active in the Union. It contains basic requirements that serve as a ***lex generalis*** regarding value chains and sustainability concerns that are not covered in one of the sectorial initiatives. For instance, deforestation in construction, mining, or environmental risks related to mining of conflict minerals would be covered by the horizontal due diligence.

This initiative also **clarifies that** in case of human rights or environmental harm in a company's value chain, **the company can be held liable** under specific conditions. Civil liability is an **effective tool for ensuring compliance** with the due diligence rules whilst at the same time **enabling victims of adverse impacts to seek remedy**. **None of these existing or planned instruments include civil liability.** Consequently, the problem of the lack of companies' accountability for adverse impacts occurring in their value chains that this initiative seeks to address would only be partially addressed by the sector-specific due diligence requirements included in existing and planned EU legislation.

Furthermore, it is expected that the package of measures adopted under the **European Green Deal** will create a regulatory environment that **encourages the green transition of companies and responsible business behaviour** within Europe, more broadly.

Several initiatives of the European Green Deal will materialise over the next years. They include legislative and non-legislative measures, notably the Fit for 55 package aiming to reduce greenhouse gas (GHG) emissions within the Union, the Zero Pollution Action Plan (including the chemicals strategy for sustainability towards a toxic-free environment), the EU Biodiversity Strategy for 2030 and the Farm-to-Fork Strategy. The different measures aim to make the EU climate-neutral by 2050 and to preserve the EU's natural environment and biodiversity. Together with Sustainable Finance Strategy, especially the proposal for a Corporate Sustainability Reporting Directive, the Sustainable Finance Disclosures Regulation and the Taxonomy Regulation, they **will have concrete impact in some areas** and **might raise awareness** about external impacts of companies' operations in others.

This initiative will further contribute to the goals of the European Green Deal, as it covers a **broad range of environmental adverse impacts**, which **companies will be expected to effectively mitigate**, including impacts generated **in value chains outside the Union's territory**.

It is **complementary to the Fit for 55 package**. Its centrepiece, the EU Emissions Trading System (ETS), covers the most carbon-intensive industrial sectors, transport and buildings. However, the **EU's external climate footprint** is not covered, save for

proposed border adjustment limited to leakage-prone ETS sectors. The same is true for other environmental concerns tackled by the Green Deal. For instance, the actions under the **Zero Pollution Action Plan** do not include any concrete requirements for companies that would lead to a reduction of the **EU's external pollution footprint**. Besides, the proposed measures under the above-mentioned EU strategies **do not cover all industry sectors and wide range of potential adverse impacts on the environment** that are covered by this initiative. This initiative is one of the concrete action points in the action plan of the **Farm-to-Fork Strategy** that could **deliver tangible results in making agricultural and food value chains outside the EU sustainable**. Apart from the proposal for a Regulation on deforestation-free products, this initiative is also a specific action in the **action plan of the Biodiversity Strategy** that could require companies to contribute to **the post-2020 biodiversity framework.**

4.3. Links with relevant international conventions, trade policy and development support measures

The Regulatory Scrutiny Board Opinion pointed to the need for more precision on the selected international environmental conventions in the "material scope" (i.e. what is covered) . To this end, the proposal does not simply put forward a list of international conventions to be covered by due diligence duty (as has been done in the Annex to the impact assessment), but **explicitly identifies a list of concrete violations of the relevant international agreements**, following a strict selection based on the need to ensure clear obligations for companies and legal certainty for EU and non-EU operations.

With regard to the Paris Agreement, **companies** (in Group 1) **would be required to adopt a plan to ensure they contribute to reaching the Union's climate commitments**, building on the disclosures under the proposed Corporate Sustainability Reporting Directive (see details in the section on the material scope) and adapt the remuneration of directors thereto. This approach reflects that companies play an important role in delivering on those goals and that it is a shared effort among public and private sectors.

Regarding biodiversity, negotiations on updating existing global standards are currently ongoing (Post-2020 Global Biodiversity Framework to the UN Convention on Biological Diversity). While **it is expected that this process would lead** to **setting action targets for 2030, including for businesses to reduce their biodiversity-related impacts**, implementation in different countries could be varied, in line with the differences in political commitments and capacities.[13]

Global trade policy has been used to address human-rights abuses and progress has been achieved in including environmental matters in trade agreements, too. The **bilateral**

[13] Target 15 aims for all businesses (public and private, large, medium and small) to assess and report on their dependencies and impacts on biodiversity, from local to global, and progressively reduce negative impacts, by at least half and increase positive impacts, reducing biodiversity-related risks to businesses and moving towards the full sustainability of extraction and production practices, sourcing and supply chains, and use and disposal, see First draft of the post-2020 global biodiversity framework (cbd.int), p. 7.

trade agreements of the EU, and of the US, **have increasingly included labour-related provisions**, for instance on forced labour, child labour and employment discrimination. This said, **effective enforcement remains an issue**.

The Commission plans to **reinforce further the sustainability dimension of existing and future trade agreements** and **to strengthen the enforcement** of trade and sustainable development commitments. At the same time, as announced in the Trade Policy review, **EU legislation on corporate sustainability due diligence is considered to be an important initiative to promote sustainable and responsible value chains**. As regards **unilateral trade instruments**, the Union is reviewing its Generalised Scheme of Preferences (GPS) also to strengthen further the scheme's contribution to sustainable development and compliance with international human rights and labour standards, environmental protection, and good governance in the beneficiary countries.

These trade policy measures will create synergies with companies' due diligence in the value chain.

3. CHANGES TO THE PREFERRED OPTION

This section first recalls the content of the preferred option identified in the impact assessment, then outlines how – after having reflected on the comments of the Board concerning in particular proportionality, the enforcement mechanism, clarity and the scope of the obligations (see especially general comments 2 and 4, and specific comments 3 to 11, 16 and 17) – the preferred option was adapted to become more focused in content and targeted in scope. For more details, please also see the Explanatory Memorandum which covers this in the section on the impact assessment.

4.4. Preferred option in the impact assessment

In the impact assessment, the presented preferred option was a combination of either option 3a or option 3b for corporate due diligence and of option 3 for directors' duties.

The preferred option for the **corporate due diligence obligation** covered three groups of companies:

- **Group 1** comprised EU very large limited liability companies that have more than 500 employees or net generate a turnover of at least EUR 350 million (sub-option 3a) or companies that have more than 500 employees and generate at least EUR 150 million net turnover (sub-option 3b).
- Under both scenarios, **Group 2** consisted of companies not included in Group 1 but having more than 50 employees and more than EUR 8 million net turnover (midcaps and medium-sized companies) and operating in high-impact sectors. These companies were also proposed to be included in the personal scope of the initiative, however, with more targeted due diligence obligations.
- **Group 3** included third-country companies which generate a significant turnover at the EU market, however, the level of this turnover was not further specified. In

terms of enforcement, **both administrative supervision and civil liability** were part of the preferred option.

Directors' duties in the preferred option 3 presented in the impact assessment included the following duties:

- The **general duty** to take into account the interests of stakeholders when acting in the interest of the company: this was proposed to apply to all EU limited liability companies.
- **Specific duties (i) to identify stakeholders, dependencies of the company from such stakeholders, and sustainability related risks to the company itself, (ii) to manage such sustainability risks, (iii) to incorporate stakeholders' interest and sustainability aspects (risks, opportunities, impacts) in the corporate strategy, and (iv) to engage with stakeholders:** these were proposed with a scope covering all large and all (non-micro) listed companies, i.e. all companies covered by the proposal for a Corporate Sustainability Reporting Directive (CSRD), as well as medium-sized high-impact companies, with a phased in application for SMEs.
- **The specific duty to set up and implement due diligence processes and measures:** this was proposed to apply to the same companies as those falling under the scope of the corporate due diligence obligation (see above).
- The **duty to include in the strategy science-based targets** regarding the mitigation of greenhouse gas emissions was proposed to apply only to large companies with more than 1000 employees.

Finally, the preferred option also included possible measures on **directors' remuneration**, namely a **general clause** applicable to all companies under the scope **to ensure that remuneration schemes facilitate or at least do not hinder compliance** with the due diligence and directors' duties.

4.5. Material scope of the proposal

The material scope of the revised preferred option (i.e. the content of the obligations) is structured mainly upon the **corporate sustainability due diligence obligation.**

It also covers obligations for the companies in Group 1 to **combat climate change. For that purpose companies 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. Within the plan they should identify the extent to which climate change is a risk for, or an impact of, the company's operations. If this risk or impact are considered principal for the company, the company should also establish emission reduction objectives in its plan.

Directors' duties were changed. While most of the duties are closely linked with the due diligence obligations and necessary for the due diligence to be effective, they also include the clarification of how directors' are expected to comply with the duty of care to act in the best interest of the company. The harmonised directors' duties include the

following elements:

- complying with the duty of care by also taking into account the human rights, climate and environmental consequences, including in the short, medium and long term, of their decisions;
- setting up and overseeing the company's various due diligence actions and, in particular, the due diligence policy, duly taking into account relevant input from stakeholders and civil society organisations. It is spelled out that the directors shall report to the board of directors on these issues;
- adapting the corporate strategy to take into account the company's adverse human rights and environmental impacts and the steps needed to mitigate them.

The specific duty to identify stakeholders' interests and dependencies of the company on such stakeholder interests are **not specified as a separate duty** in the proposal (but are implicitly included in the clarified duty of care). The broader duty to manage risks to the company related to stakeholders and their dependencies, as well as the broader duty to include the management of sustainability risks to the company in the corporate strategy (going beyond the requirement to specify indicative emission reduction objectives in case climate change is a principal risk to, or a principal impact of, the company) were not retained. Similarly, the specific duty to set up and oversee the implementation of processes related to the management of sustainability risks to the company, and the mandatory adoption and disclosure of science-based targets were not retained either.

As regards **directors' remuneration**, the proposal specifies for the group 1 that the company's plan to ensure that its business model and strategy are compatible with the transition to a sustainable economy and to the EU's climate commitments is duly taken into account in directors' variable remuneration.

The **due diligence obligations** cover human rights[14] and environmental adverse impacts on the basis of **defined provisions of selected international conventions (as universal legal standards) which include precise and specific rights and obligations** that are to be respected by **companies**. The due diligence obligations require companies to identify and take appropriate measures to prevent and mitigate adverse human rights and environmental impacts. The **Annex to the proposal contains details about the content of selected human rights** (Part I Section 1), and clarifies that the violation of a right not listed there but protected by the human rights agreements listed in the same Annex (Part I Section 2) is also covered as long as the violation is directly capable of impairing a protected legal position in a particularly serious manner, and if the impairment of the protected right is obvious upon reasonable assessment of all circumstances in question.

[14] 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.

As regards environmental adverse impacts, the Annex (Part II) **identifies relevant violations of internationally recognized objectives and prohibitions included in environmental conventions**.

The **environmental due diligence obligations were reassessed in view of other EU regulations in this field** and the need to outline obligations for companies in a clear manner to ensure legal certainty. **Only those environmental conventions[15] which create an obligation that is sufficiently precise and implementable for the companies** have been maintained but they have been extended.

Stakeholders' involvement was limited to what is necessary for the due diligence, also taking into account the OECD Guidelines and the practice followed by companies when implementing these Guidelines. **Directors should take into account the input from stakeholders and civil society associations when** putting in place and overseeing the due diligence actions and in particular the due diligence policy, i.e. the company's strategy on how to implement due diligence, including in the long-term and its prevention and correction action plan, where relevant. The company will also be required to operate **a complaints mechanism** as part of due diligence which would allow stakeholder-complainants to bring potential adverse impacts to the attention of the company. This will further enable the companies to get a knowledge of possible risks of adverse impacts and of how their impact mitigation strategy works on the ground.

Directors' duties closely linked to the implementation of due diligence have been kept, in line with the international voluntary due diligence frameworks and standards that also cover due diligence governance. **It allows due diligence to become strategic and to infiltrate into relevant corporate functions**. A due diligence obligation without a proper corporate governance backing and without directors' responsibilities could become a mere compliance issue of secondary relevance. **Regulating directors' duty of care was retained**.

Voluntary due diligence systems and existing national due diligence laws also contain directors' duties, both (1) **to ensure a strategic approach** on due diligence and (2) **to embed due diligence into corporate management systems**. For example:

- The **UN Guiding Principles on Business and Human Rights** state that "as the basis for embedding their responsibility to respect human rights, business enterprises should express their commitment to meet this responsibility through a statement of policy that: (a) [i]s approved at the most senior level of the business

[15] The Minamata Convention on Mercury; the Stockholm Convention on Persistent Organic Pollutants; Convention on the Prior Informed Consent Procedure for Certain Hazardous Chemicals and Pesticides in International Trade; the Vienna Convention for the protection of the Ozone Layer and its Montreal Protocol on substances that deplete the Ozone Layer; the Basel Convention on the Control of Transboundary Movements of Hazardous Wastes and their Disposal, Convention on Biological Diversity; Convention on International Trade in Endangered Species of Wild Fauna and Flora.

enterprise (…) [and] (e) [i]s reflected in operational policies and procedures necessary to embed it throughout the business enterprise"[16].

- According to the **OECD Due Diligence Guidance for Responsible Business Conduct (RBC)**, as step 1 of the due diligence process, companies are recommended, among others, to "[d]evise, adopt and disseminate a combination of policies on RBC issues", "embed the enterprise's policies on RBC issues into the enterprise's oversight bodies" and embed these also "into management systems so that they are implemented as part of the regular business processes", and as practical action, to "assign oversight and responsibility for due diligence to relevant senior management and assign board level responsibilities for RBC more broadly"[17].
- The **German Act on Due Diligence Obligations in the Supply Chains**[18] states that if an enterprise identifies a risk (i.e. of adverse impact) it must issue a policy statement on its human rights strategy. Senior management must adopt the policy statement.
- The **French Duty of Vigilance Law** requires the due diligence plan to be published as part of the management report of the company, which is the responsibility of the management. In addition, the French *Loi Pacte*[19] clarifies the duty of care of directors as follows: "*The company is managed in its corporate interest, taking into consideration the social and environmental issues related to its activity*".

4.6. Personal scope of the proposal

The personal scope (i.e. which business categories, and the directors of which business categories are covered) **has been revised to better ensure proportionality and adequate implementation.**

On the one hand, the due diligence obligation will remain to be targeted to companies that have larger operations, or are somewhat smaller in size but operate in sectors where adverse external impacts were identified to be more frequent or significant. Such companies are **more likely to contribute to potentially significant adverse impacts**, including in their value chains. On the other hand, the turnover criteria is also a proxy for the influence in the value chains (as used in the EU Directive 2019/633 on unfair trading practices in the agricultural and food supply chain[20]). Furthermore, combined with the criterion on the number of employees, it can ensure that the due diligence obligation is targeted well at those companies – operating at the various levels of the value chain –

[16] Guiding Principles on Business and Human Rights, Operational principles, policy commitment, point 16., GuidingPrinciplesBusinessHR_EN.pdf (ohchr.org)
[17] OECD-Due-Diligence-Guidance-for-Responsible-Business-Conduct.pdf, page 23.
[18] Section 6, preventive measures.
[19] La loi PACTE : pour la croissance et la transformation des entreprises | economie.gouv.fr
[20] Directive (EU) 2019/633 of the European Parliament and of the Council of 17 April 2019 on unfair trading practices in business-to-business relationships in the agricultural and food supply chain; https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32019L0633

that **have the required influence and also the corresponding resources to properly conduct due diligence**.

A **very recent study on the uptake of corporate social responsibility (CSR) and sustainability practices among European SMEs**[21] confirms that SMEs may face constraints to conduct due diligence in practice because they **lack the resources** to monitor their value chains and to investigate beyond their direct suppliers. Furthermore, this should be looked at in the context of the COVID-19 pandemic which has hit SMEs particularly hard. Meanwhile, SMEs are also commonly **on the receiving end of value chain policies** as they are often part of value chains.

Taking all these considerations into account, it was decided to **fully exclude SMEs and smaller midcap companies from the scope of application** of the proposed legislation. However, it still includes larger midcap companies active in economic sectors where the risk of significant adverse human rights or environmental impact is particularly high.

The division of the scope into **two main groups of EU companies** have been maintained. Group 1 has remained the same as it was in the more restrictive sub-option of the impact assessment's preferred option (option 3b) that defined very large companies combining the number of employees and the worldwide net turnover size criteria cumulatively (i.e. dropping the other preferred sub-option, option 3a, in which the two criteria were not used cumulatively). Group 2 has been adapted and better targeted both in terms of the size and the sector of the companies it comprises. As a result, the number of companies in this group has been reduced substantially compared to either of the two preferred sub-options of the impact assessment. Accordingly, the **revised and more targeted preferred option covers:**

- *Group 1:* large EU limited liability companies with more than 500 employees and more than EUR 150 million worldwide net turnover ("very large companies" as defined in option 3b of the draft impact assessment), irrespective of the sector in which they operate, and
- *Group 2:* large EU limited liability companies that do not simultaneously reach both thresholds of Group 1 but have more than 250 employees and more than EUR 40 million worldwide net turnover ("midcap large companies")[22] and that have the majority of their operations in high-impact sectors (which are now also based on a narrow definition, as explained hereunder). For these companies, the obligations will be lighter and phased in (see the next point on proportionality).

Moreover, **the approach to selecting high-impact sectors has been changed to focus on sectors for which relevant OECD guidance already exist**. The selection of these sectors reflects the priority areas of both national and international action aimed at tackling human rights and environmental issues. These are sectors in particular

[21] European Commission, Executive Agency for Small and Medium-sized Enterprises, *Uptake of corporate social responsibility (CSR) by European SMEs and start-ups: final report*, Publications Office, 2021,
[22] Note that the category of "midcap large companies" is narrower than the "midcaps" of option 3b of the impact assessment.

characterised by high risk of human rights violations (e.g. forced labour, worst forms of child labour)[23] as better explained in Annex 11 of the Impact Assessment. Such guidance currently covers the minerals supply chains – with additional guidance on the extractive sector –, the agricultural, and the garment and footwear supply chains. OECD guidance also exist for companies in the financial sector with respect to their lending and securities underwriting services and to their activities as institutional investors. However, due to its specificities, a different approach is followed with regard to this sector: instead of covering more midcap limited liability companies, the proposal covers more of the very large companies in this sector, including also those that do not have a legal form with limited liability (e.g. cooperative credit institutions and insurance companies). Covering financial sector companies that were established in a different legal form is also in line with the scope of sustainability reporting rules under the CSRD proposal.

Group 1 consists of **9 400** very large companies (same as in option 3b of the impact assessment). However, as a consequence of the changed approach to the selection of high-impact sectors, and due to excluding all SMEs and smaller midcaps from the scope completely, the estimated number of companies in Group 2 that will be covered only if they operate in high-impact sectors (i.e. taking into account that about 30% of Group 2 companies are already indirectly covered as subsidiaries of larger companies) is estimated to be reduced from about 34 600 (in option 3b) to approximately **2 300** companies.[24]

Given the changes in Groups 1 and 2, **the number of companies in the scope of the Directive which will incur incremental compliance costs is reduced** from 44 000 in the less extensive preferred option (option 3b) **to 11 700** in the proposal.

The changes and the estimated number of EU companies covered in the proposal is summarised in the following table:

[23] For instance, the OECD's guidance "Practical actions for companies to identify and address the worst forms of child labour in mineral supply chains" points out that, out of the 139 goods on the 2016 List of Goods Produced with Child Labor or Forced Labor (TVPRA) compiled by the United States Department of Labor's (USDOL), 29 goods are in minerals and quarrying.

[24] In line with the methodology of the impact assessment, this figure already accounts for the group effects as it takes into account the assumption – explained in the impact assessment – that about 30% of midcap companies will already be indirectly under the scope as a subsidiary of a larger parent company in any case and, as such, their compliance costs are already included in the aggregate cost estimate. The total number of companies that are directly covered by the scope if operating in a high-impact sector has been reduced from about 49 500 (in option 3b of the impact assessment) to approximately 3 400, as shown in the table below.

Our estimate includes limited liability companies involved in the following economic activities: (i) extraction and mining of natural resources (crude petroleum, natural gas, coal, lignite, metal ores and other, non-metallic minerals and quarry products), (ii) certain other activities in the upstream minerals supply chains (in particular the wholesale of metals, ores, construction materials, fuels, chemical and other intermediate products, and the manufacture of basic metal products, of other non-metallic mineral products and of fabricated metal products, except machinery and equipment), (iii) agriculture, forestry and fisheries, the manufacture of food products and beverages, and the wholesale trade of agricultural raw materials and live animals, wood, food, beverages, as well as (iv) the manufacture of textiles, wearing apparel, leather and related products (including footwear), and the wholesale trade of textiles, clothing and footwear. Companies involved in the retail sector are excluded for the purposes of these calculations.

Number of companies	Option 3a	Option 3b	Proposal
Group 1	23 300	9 400	9 400
Group 2 (100%)	46 700	49 500	3 400
Total number of EU companies directly under the scope	70 000	58 900	**12 800**
Total number of EU companies incurring incremental compliance costs (i.e. accounting for group effect)	56 000	44 000	**11 700**

In addition, **the approach and the thresholds to cover third-country companies are now better aligned with those applied to EU companies**. As a result, third-country companies will be covered if they generate a net turnover in the Union of more than EUR 150 million, or less than that but more than EUR 40 million in case they have the majority of their operations in high-impact sectors.

Reflecting on the Board's opinion, the Commission also estimated the **number of third-country firms** that would fall under the scope irrespective of their sector of economic activities. For this, a simple log-linear model was used calculating the number of firms as a function of their estimated[25] intra-EU27 annual turnover[26]. According to the model, if the threshold is set at EUR 150 million annual EU turnover, the scope covers a little less than **2 600** non-EU companies. Assuming that the number of midcap large companies in high-impact sectors compared to their number in all sectors[27] would be the same as in the case of EU companies (about 20%), an additional **1 400** non-EU companies with an EU turnover of EUR 40 to 150 million will fall under the scope if they are active in high-impact sectors.[28,29]

[25] The turnover in the model is the sum of the remunerations of factors of production (labour, capital) augmented by a profit margin that is a proxy for the degree of competitiveness of markets that firms operate in. Firm-level data from the ORBIS database were used to find comparable values for the labour-capital shares and profit margins in the EU27.

[26] The model is based on the trade figures with the EU's three major trading partners for which firm-level data are reported: Switzerland, the UK, and the U.S. It takes the average value of the three estimates based on the respective trade shares. It uses OECD data (including the Trade by Enterprise Characteristics database for the UK and Switzerland, which reports the number of trading firms for different size categories, including by number of employees and trading volumes).

[27] In the model, the threshold of EUR 40 million turnover corresponds to 9 600 non-EU companies, resulting in about 7 000 non-EU midcap large companies in all sectors.

[28] These are based on 2017 data. Depending on the data source for the U.S. firm-level data, the model can be also be estimated for 2019, the results being very similar. If the threshold is decreased to EUR 100 million, almost 4 000 companies would be covered, if it is increased to EUR 250 million, the number of companies covered would be about 1 500.

Sensitivity analysis: We used the following parameter values: wage share=0.54, profit margin=8%, weight of job rich industries=0.8. The number of firms increases with respect to the profit margin, and decreases with respect to the wage share and the weight of job rich industries. Setting the profit margin to 15% and lowering the share of job rich industries to 50%, the number of firms in scope increases to more than 3 400 for the 150 million threshold. In the other direction, increasing the wage share to 80% and lowering the profit margin to zero, the number of firms for the same threshold falls below 1 600.

[29] The plausibility of this estimation was cross-checked with data reported by the American Business Chamber and also by using data on foreign direct investment flows and international investment positions.

4.7. Enforcement mechanism

The Board considered that policy options not including civil liability regime should have been assessed as "*stakeholders consider administrative supervision as the preferred option and this seems a solution also introduced at Member State levels*".

In the open public consultation, stakeholders who indicated that they were in favour of administrative supervision were not necessarily against an accompanying civil liability regime.[30] At the same time, various position papers from business associations and individual companies where asking to either exclude civil liability or limit it to tier-1.

Existing **due diligence laws in two Member States do not exclude civil liability** regimes for corporate due diligence. The French *Loi sur le Devoir de Vigilance* expressly stipulates that civil liability rules are applicable, while the German *Lieferkettensorgfaltspflichtengesetz (LkSG)* clarifies that violation of the obligations under that law does not as such give rise to civil liability but also that (generic) civil liability arising from a damage derived from one of the violations covered by the new law remains unaffected.[31] The German civil law includes generic civil liability rules that remain applicable in case of the violation of a protected right.

Moreover, **access to effective remedy for the victims is a core component of the UN Guiding Principles on Business and Human Rights (UNGPs)**. The complementarity of civil liability and administrative supervision in developing robust enforcement approaches has recently been identified by the UN Working Group on Business and Human Rights as one of the priority areas on which States should focus on when implementing the UNGPs.[32]

An enforcement mechanism based on administrative law and a complementary civil law mechanism is **used also in other areas of Union law, notably in competition law**. Below are further considerations as to why **an enforcement regime with tailored rules for civil liability significantly increases the effectiveness of enforcement** as compared to a regime without express rules on civil liability.

First, civil liability is an **effective tool for ensuring compliance** with the corporate due diligence rules while providing legal certainty for companies. Being **independent from supervisors' capacities and priorities** in pursuing infringements of the due diligence obligation, it can complement Member State's supervision in making the enforcement

[30] In fact, 320 out of the 555 respondents choosing the option supervision, i.e. 58% of them, also chose the option judicial enforcement with liability and compensation in case of harm caused.

[31] Section 3(3) stipulates that "[a] *violation of the obligations under this Act does not give rise to any liability under civil law. Any liability under civil law arising independently of this Act remains unaffected*."

[32] See the "UNGPs 10+" Roadmap for the Next Decade of Business and Human Rights (November 2021, ohchr.org), a stocktaking by the UN Working Group on Business and Human Rights of the first decade of implementation of the UNGPs, complemented by forward-looking recommendations (priority goals for States, businesses and other key stakeholders) for the next decade in key action areas.

regime **more effective and deterrent**. It has been shown that **civil liability makes a difference in positively driving good corporate behaviour**.[33]

Second, a clearly defined and proportionate civil liability regime **offers legal certainty**[34] **for both companies and affected persons**, and **a more effective remedy to victims** of adverse impacts. Companies would know what is expected from them as they may already be sued before courts for contributing to harm. As regards victims, civil liability **can result in different remedies besides financial compensation**. Victims could ask the court for **remedial orders** such as clean-up orders, restitution of land, etc.

Furthermore, the proposal requires Member States to ensure that victims of human rights and environmental harms are **not denied the protection** that is granted in accordance with the relevant provisions on due diligence of the Directive where the law applicable to such claims is not the law of a Member State. For example, victims would benefit from the protection, under certain conditions, **when the relevant damages** caused by the failure by the company to respect the due diligence obligations **occur outside of the Union**. Also, if there is a dispute and litigation, this solution would **provide legal certainty and facilitate the work of the Union courts**, as they can apply the law of their own country (i.e. the law of the country in which an action is brought, *lex fori*) instead of foreign law.

The provision on civil liability included in the proposal is **in line with the existing civil liability rules in Member State laws whereby a person who has caused harm to another person has to repair that harm**.[35]

With a view to make clear how civil liability should apply to harm at the level of **indirect relationships**, the proposal sets out **clearly defined conditions** under which companies may be held liable for such harm. It is clarified that

- civil liability only applies with respect to **established business relationships**, which requires an element of duration and intensity;[36] and that
- the company can only be held liable **if it did not take appropriate measures** required by the proposal,

[33] See Steering CSR Through Home State Regulation: A Comparison of the Impact of the UK Bribery Act and Modern Slavery Act on Global Supply Chain Governance - LeBaron - 2017 - Global Policy - Wiley Online Library; The importance of civil liability for a corporate human rights duty - (unl.pt); Transnational Legal Activism in Global Value Chains - The Ali Enterprises Factory Fire and the Struggle for Justice, see e.g. at p. 155; Wettstein & Schrempf-Stirling, Journal of Business Ethics Oct. 2017, Human Rights Litigation and its Impact on Corporations' Human Rights Policies.

[34] The proposed civil liability in the legal text concerns only established business relationships with which a company has regular and frequent cooperation and applies only where the adverse impact could have been foreseen, prevented, ceased or mitigated with appropriate due diligence measures. As it will in practice be difficult to prevent all risks through global value chains, liability is limited to harm done in the value chain under specific conditions especially beyond direct suppliers.

[35] For the sake of clarity, the provision on civil liability in the proposal will not give stakeholders the right to sue competent authorities if they find that enforcement is not sufficiently strict. It aims at establishing liability of the companies within the scope of the proposal.

[36] According to the proposal, established business relationships are direct and indirect business relationships which are, or which are 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.

- at the level of indirect business relationships if it the company used contractual cascading and assurance as well as measures to verify compliance with it should not be liable, 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,
- Furthermore, the proposal clarifies that, when assessing liability and its extent, due account should 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 as well as any collaboration with other entities to address adverse impacts in its value chains.

The Directive is **not expected to give rise to an affluence of damages claims**. First, the **experience with the French** *Loi de devoir de vigilance* has shown that the Law has not led to a multitude of claims for damages after its entry into force.[37] Second, **past EU legislation** introducing civil liability regimes or facilitating claims have not led to a strong increase in frivolous cases before national courts.[38] Third, key elements such as **the entity legitimated to bring an action**, the **burden of proof** would **not be changed** by this proposal. In addition, bringing an action **may require considerable financial resources**, which will be a **disincentive against ungrounded claims**.

In order to ensure that remedy can be sought effectively, the civil liability regime is complemented by a provision according to which the liability provided for in provisions of national law transposing the relevant provision on civil liability must be of **overriding mandatory application** in cases where the law applicable to claims to that effect is not the law of a Member State.

In response to the Board's comment that the impact assessment should better explain which national authority would be best placed to act (including with respect to third-country companies), this section also provides further information on the choice of supervisory authority. According to the proposal, **Member States are free to designate one or more authorities** for the purposes of supervising compliance with the proposed Directive. It is for the Member States to decide which authority or authorities to designate, and they may include an authority that is not traditionally supervising compliance with corporate governance rules. It is possible that such "traditional" supervisory authorities will not be selected by Member States, although they may choose them. Where competent authorities under sectoral legislation exist, Member States could identify those as responsible for the application of this Directive in their areas of

[37] https://www.vie-publique.fr/sites/default/files/rapport/pdf/275689.pdf

[38] E.g. the Damages Directive for infringements of competition law (Directive 2014/104/EU) or application of the 2013 Recommendation on the Collective Redress. If there has been increase of justified claims, this demonstrates that the awareness of victims of their right to effectively claim damages has enhanced, e.g. see Commission Staff Working Document (2020)338.

competence. They could designate authorities for the supervision of regulated financial undertaking also as supervisory authorities for the purposes of this Directive.[39]

4. ASSESSMENT OF IMPACTS

This section addresses the comments of the Board that the impact assessment should be more balanced and should better account for potential negative impacts in third countries and for potential impacts of the proposal on competition and competitiveness of EU companies. It also contains the recalculated cost estimates as suggested by the Board, additional considerations regarding cost, benefits and proportionality (See Annex: Overview table, General comment 3 and Specific comments 12 to 16).

4.8. Revised cost assessment

As the scope of the proposal is significantly smaller than the scope of the preferred option in the impact assessment, the **aggregated direct compliance costs for EU businesses** implied by this directive **were recalculated**.

As explained in Annex 4 of the Impact Assessment Report, total direct compliance costs comprise the incremental substantive compliance costs and the incremental administrative costs.[40]

Substantive compliance costs consist of two main elements: (i) the "**procedural costs**", i.e. costs of setting up and operating due diligence processes and procedures and (ii) the **transition costs** – the investment needs – of harm mitigation and of transitioning the company to sustainability. The impact assessment only quantified the procedural costs (pointing out that the transition costs, on the long run, can even be zero or become profitable investments). With the new personal scope and using the relevant firm-level costs estimated in the impact assessment, these costs for all **EU businesses** covered are now estimated to amount to **EUR 760 million recurrent** and **220 million one-off** costs (down from EUR 1.72 billion and 500 million, respectively, in option 3b of the impact assessment).

As regards **administrative costs**, these are **linked to reporting to the public**. While this is an important element of the due diligence framework, all companies covered under the new scope will already be required to disclose to the public sustainability and due diligence-related information in accordance with the Corporate Sustainability Reporting Directive (which, according to the Commission's 2021 proposal, will apply to all large

[39] For instance, in Germany, the Federal Office for Economic Affairs and Export Control is responsible for the supervision of the German Act on Corporate Due Diligence in Supply Chains. The Office is not responsible for tasks related to corporate governance. It is entrusted with administrative tasks in relation to foreign trade, promotion of economic development and SMEs, energy, auditor oversight, BAFA - Tasks: https://www.bafa.de/EN/Federal_Office/Tasks/tasks_node.html.

[40] Please note that the Impact Assessment was prepared on the basis of the Better Regulation Guidelines and its toolbox as in force at the time, and this document retains the same methodology used by the impact assessment for classifying and assessing the various cost elements. Nevertheless, the summary of benefits and costs of the preferred option is presented here (in Annex 2) according to the recently updated guidelines and the new template for the table(s), with a separate table prepared for the implementation of the One In One Out Principle.

EU companies and all companies listed in the EU, i.e. a broader scope of EU companies than this initiative). The CSRD has been taken into account in the dynamic baseline of this initiative. Thus, **companies will already face most of the administrative costs** (namely the cost of reporting, as well as data gathering and analysis underpinning this reporting)[41] **under the CSRD**. This is why with the reduced scope EU companies **will not incur any substantial additional administrative costs under this directive**. This is reflected in the summary table of the expected benefits and costs presented in Annex 2, in particular in the table on the **"one-in-one-out" principle**.

Non-EU companies are estimated to incur **EUR 240 million recurrent and 70 million initial procedural compliance costs** (using the newly estimated number of companies under the scope and the relevant firm-level costs estimated for large EU companies in the impact assessment).

The following table summarises the total compliance costs for EU and non-EU businesses (except for transition costs) under the previous two preferred sub-options and the final proposal:

Aggregated compliance costs for EU companies (without transition costs), in EUR	Option 3a	Option 3b	Proposal
recurrent	2.37 bn	1.72 bn	0.76 bn
one-off	0.68 bn	0.50 bn	0.22 bn

Aggregated compliance costs for non-EU companies (without transition costs), in EUR	Option 3a	Option 3b	Proposal
recurrent	Not calc.	Not calc.	0.24 bn
one-off	Not calc.	Not calc.	0.07 bn

In line with the reduced personal scope of the corporate due diligence obligation, the **supervisory costs** incurred annually by existing or newly set up public authorities that will be designated by Member States to monitor and enforce compliance **will also be lower** than in the two preferred sub-options of the impact assessment. Following the calculation method explained in Annex 4 of the impact assessment, the **total recurring supervisory costs in the EU** are estimated to reach about **EUR 5.55 million a year**, and the **initial costs** will be about **EUR 130 000**. The following total annual and initial costs are estimated:[42]

[41] Note that the impact assessment assumed that about half of the costs of data gathering and analysis that companies incur in relation to their reporting obligations overlaps with their costs incurred in relation to their due diligence obligations. On average, such overlapping costs decrease the data gathering and analysis costs estimated by the impact assessment to be incurred under this initiative by about one third.

[42] The impact assessment does not count with additional costs for courts implied by the possibly increased number of lawsuits: while it is difficult to predict how many cases the courts will have to deal with, the cost of civil court procedures are anyway paid by the parties involved. Estimating the number or cost of

Total supervisory costs in EU, in EUR	Option 3a	Option 3b	Proposal
recurrent (EU companies)	11.24 mn	7.86 mn	4.42 mn
recurrent (non-EU companies)	Not calc.	Not calc.	1.13 mn
one-off	0.13 mn	0.13 mn	0.13 mn

4.9. Proportionality

As explained above, **SMEs and smaller midcap companies are not included** in the scope of application of the proposed legislation, resulting in much lower direct compliance cost for the businesses and lower supervisory costs for the public authorities. However, SMEs are often involved in the upstream supply chains of larger companies. Thus, even if they are not required to set up self-standing due diligence mechanisms, **they will be indirectly affected by the due diligence undertaken by larger "buyer" companies and need to participate in such due diligence steps**.[43]

The Commission has considered carefully how to further support SMEs, in order to tackle the indirect negative effect of a due diligence legislation on SMEs.[44] For example, **large "buyer" companies will be encouraged to provide targeted support**, including financial support for independent on-site checks on suppliers in their value chains and not to have unfair and disproportionate requirements from their SME business partner. Furthermore, **a strong package of support actions**, including e.g. model contractual clauses, hotlines, trainings and databases, an observatory for supply chain transparency, development policy projects, alignment methodology for self-assessment of industry schemes and multi-stakeholder initiatives, and other public support **at Member State and EU level** can also play a role in assisting SMEs in the EU and in third countries.

For midcap companies that will be covered by the proposal if they are active mainly in one of the identified high-impact sectors, **the due diligence obligation will be simplified:** they would only have to **focus on severe adverse impacts only**.

Midcap companies in Group 2 will also have more time to adapt thanks to the **phased-in implementation**: they would need to apply the rules only 2 years after the entry into force of the proposed Directive. This additional time does allow these companies to **smooth out the costs** of establishing the necessary processes and procedures. The delayed application could further alleviate their burden, if **industry cooperation improves** in the meantime, or **technological developments, standards, etc. become available or cheaper**, which may also be prompted by the earlier implementation date for larger companies.

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court cases initiated by victims whose complaint was not pursued by the supervisory authority and therefore go to court would be highly hypothetical.

[43] The study shows that this can have a positive impact on sustainability uptake in smaller companies, but can also be perceived as coercion and increase the costs and administrative burden of SMEs.

[44] Note that the estimated direct business compliance costs also include the costs incurred by large companies conducting due diligence also with regard to their value chains.

Taking into account the various impacts, the revised preferred option allows for reducing business' compliance costs substantially and also for lowering the supervisory costs, while only decreasing the effectiveness and the beneficial human rights and environmental impacts of the initiative to a relatively lower extent, **making the proposal more efficient and proportionate**.[45] With respect to firm-level cost competitiveness under the revised preferred option, please also see section 4.6.

4.10. Impacts on third countries

The proposal's scope covers certain non-EU companies directly. In addition, it obliges companies to cover their global value chains in their due diligence efforts. As the most salient adverse impacts on human rights and on the environment often occur outside the EU, **the proposed Directive has a strong external dimension and will inevitably affect companies and other stakeholders in third countries, and could affect the economies of third countries more broadly**. The proposal takes into account that this requires **coherence** with the EU's trade and development policies, and measures to mitigate potential negative impacts on our partner countries. Moreover, coherence with international frameworks on Responsible Business Conduct as well on Business and Human Rights is important as it **creates synergies for companies and facilitate compliance**.

One of the main objectives of this initiative is to reduce adverse human rights and environment impacts also in global value chains[46], and corporate due diligence is an effective tool to attain such objectives. It has to be stressed that due diligence is enshrined in international frameworks and it is therefore internationally recognized as the appropriate tool to mitigate adverse human rights and environmental impacts, including in value chains. In addition, evidence shows that when companies use **due diligence** or comparable corporate impact management tools, these are **effective in preventing or mitigating adverse impacts in their operations and value chains in third countries**. It has been shown that corporate sustainability management tools, when used on the basis of voluntary individual commitments[47] and voluntary industry initiatives[48], can have far-

[45] As the aggregate costs estimated for non-EU companies is relatively low, while expected positive impacts are relatively high, proportionality concerns do not arise in this respect.

[46] Examples of EU companies having adverse impacts in third countries can be found in the Impact Assessment Annex 11.

[47] E.g. Nestlé's Child Labour Monitoring and Remediation System (CLMRS) showed effectiveness in identifying child labour where it occurs, in supporting families to prevent children performing hazardous tasks and in providing enhanced education opportunities. Therefore, recently Nestlé has developed a Human Rights Framework and Roadmap putting due diligence at the core of the approach, with the objective of scaling positive impact for rights holders on the ground. Furthermore, Philips supplier sustainability Performance programme achieved to improve the conditions for approximately 302 000 workers, as labour conditions improved, the risk of serious injury was reduced, and the negative environmental impact of suppliers brought down. Tesco monitors in key sourcing countries that salaries are paid on time and in full for all hours worked, including overtime premiums, where relevant, and requires suppliers to pay any missed wages. In 2019/20 they identified 52 cases, affecting 7 060 workers, where payments had fallen short of what should have been paid, including premiums for overtime, that were subsequently addressed as a result of Tesco's intervention. ASOS has worked with NGOs and suppliers in Turkey to reduce risks to Syrian refugees. By 2019, it had provided 82% of Syrian refugee workers in their Turkish supply chain with work permits. Unilever ensured living wages for Brazil suppliers, and

reaching effects[49] in addressing sustainability problems. In addition, relevant **legislation** in France and the US **has been found to be effective in enhancing due diligence efforts of companies**. The French Duty of Vigilance Law was found to have triggered "*internal mobilisation around due diligence, to encourage cross-departmental cooperation and to better integrate due diligence into corporate governance*", as well as to "*professionalise*" the treatment of due diligence in corporate practices,[50] while the **US Dodd Frank act shows concentration of efforts** where legislation exists.[51]

At the same time, to date, **it is difficult to fully assess the possible negative impacts of due diligence implementation on companies in third countries** as standards have been largely voluntary. Those that have been legislated[52] are few, and have not been in effect long enough to adequately assess change on the ground. Based on the available data, **reinforcing the respect of the environment and human rights throughout value chains can have positive impacts**[53] but **may also have collateral negative impacts**. While negative impacts in third countries may not be excluded in some cases, the proposal will contain a number of safeguards with a view to mitigating such possible impacts (as explained later).

It is reasonable to conclude that this initiative will lead to **significant beneficial impacts in those third countries from which the EU imports relatively risky products or services in relatively large volumes** (i.e. where the current risk of adverse impacts linked to the imported raw materials, products, services, or to the operation of companies in the given sector in the given country is high). **Potential negative effects are also likely to be highest in these countries** and the impact on the ground may be relatively higher in developing countries.

For instance, the following tables[54] show the main trading partners of the Union (with more than 1% share in total extra-EU imports) with regard to the subgroups of imported **commodities** (also called primary goods):

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transportation is now being provided to workers. Repsol ensured the protection of indigenous peoples' rights by conducting a human rights due diligence process that concluded with the company's decision not to carry out the exploratory project due to high cultural impact on sacred spaces of the Wayuu ethnic group, with no possible mitigation measures.

[48] In terms of organised responses to the sustainability problems, the Bangladesh Accord resulted in companies having to participate in a system to identify risks as well as to induce suppliers to comply and do the necessary renovations in order to prevent risks, while the YESS initiative addressed the risks in cotton sourcing at fabric mill and spinning level.

[49] E.g. Gallup Supplier engagement research describes the benefit of supplier's engagement such as higher quality, improved planning and product development, greater supplier support and value and lower costs; CDP 2018 report on sustainable supply chain practices show that 551 million Tonnes of CO^2 have been cut by suppliers and that doing so saved these suppliers 14 billion US$.

[50] https://www.e-dh.org/userfiles/Etude%20EDH_Plans_de_vigilance_2019-2020_Decembre2020.pdf

[51] Evidence indicated that companies were conducting due diligence in relation to tin, tungsten and tantalum (3T) and gold, covered by legislation, but not in relation to cobalt which was not covered.

[52] E.g. Dodd-Frank Act in the US, Modern Slavery Act in the UK, Duty of Vigilance Law in France, Conflict Minerals regulation in the EU.

[53] E.g. Evaluation de la mise en œuvre de la loi relative au devoir de vigilance, January 2020

[54] Source: Eurostat data for 2020, see Extra-EU trade in primary goods - Statistics Explained (europa.eu) and related sites.

Raw materials (54% of all extra-EU imports of commodities): non-manufactured goods like oilseeds, cork, wood, pulp, textile fibres, ores and other minerals, animal and vegetable oils	Share of imports by partner (%)
United States	12.0
Brazil	9.9
Canada	7.2
Russia	6.2
Ukraine	6.2
United Kingdom	4.8
South Africa	4.5
Indonesia	4.4
Malaysia	2.7
Chile	2.3
Norway	2.2
Turkey	2.2
Peru	2.0
Australia	1.8
Switzerland	1.7
Mexico	1.4
India	1.3
Argentina	1.2

Food, drinks and tobacco (27% of all extra-EU imports of commodities)	Share of imports by partner (%)
United Kingdom	14.0
Brazil	7.3
United States	6.2
Norway	5.9
Turkey	4.2
Switzerland	3.8
Argentina	3.5
Morocco	3.1
Côte d'Ivoire	3.0
Ukraine	2.7
Vietnam	2.6
Peru	2.3
Ecuador	2.2
South Africa	2.0
Chile	1.9
India	1.8
Russia	1.5
Canada	1.5
Colombia	1.5
Thailand	1.4
Costa Rica	1.3
New Zealand	1.2
Serbia	1.1
Ghana	1.1
Indonesia	1.1

However, in certain sectors or commodities[55] there is lower procurement power, and EU companies may have **more limited leverage** to bring about change as the product comes only from few countries and sometimes also from a limited number of suppliers. On the other hand, because of the limited number of sources, **continuous engagement is paramount and gives strong incentives** to contribute to change. About half of imports of the products identified in Commission analysis on strategic dependencies originate in China (52%), followed by Vietnam (11%) and Brazil (5%).

There is a certain risk that those suppliers in producing countries will prefer to **sell to other regions** where due diligence rules are not in place or less stringent. At the same time, given **the Union market's size** and the **safeguards in the proposal** requiring that the EU company engages locally and contributes to the costs of new production processes, infrastructures if necessary, and shares burden with SMEs, will lower such risks.

Furthermore, a range of raw materials of relevance for the manufacturing of various goods can **only be sourced from countries with a high risk profile**.[56] This heightens the risk of EU companies abandoning certain suppliers, regions and even countries. On the other hand, **this risk of disengagement** (termination of the business relationship) **is mitigated** through the following factors and safeguards in the initiative:

[55] The Commission's analysis "**Strategic dependencies and capacities"**, accompanying the updated EU industrial strategy, has identified 137 products in sensitive sectors on which the EU is highly dependent, such as raw materials, processed materials, chemicals (these 3 categories cover 99 products out of 137), active pharma ingredients as well as other products relevant to support the green and digital transformations (batteries, semiconductors, cloud and edge technologies).

[56] Also, as explained above, the risk of certain adverse impacts is higher in specific product groups or raw materials.

- The **cost** of reorganising value chains may be higher than making it sustainable;
- The proposal does **not target specific geographies or products**. If it was, the impact would also be more pronounced for certain territories (see further in the impact assessment);
- There are **safeguards** in the proposal to ensure that disengagement is only a last resort option, such as the following:
  (1) measures ensuring that the **emphasis is on preventing and mitigating** adverse impacts, rather than banning certain products originating from certain areas,
  (2) prevention and mitigation should include proper investments, where necessary,
  (3) prevention and mitigation should include targeted financial or other support for the SME trading partner, where necessary,
  (4) collaboration with other entities, including, where relevant, to increase the company's ability to bring the adverse impact to an end,
  (5) termination of the business relationship only if the potential adverse impact is severe, and where the law governing their relations so entitles companies to do so.
- **Collaborative efforts** will also be fostered through support measures and through industry schemes and multi-stakeholder initiatives.
- The proposal is also likely to **incentivise third-country governments** to strengthen rule of law, improve legislation, enforcement and good governance practices that support sustainable development.

Furthermore, it is important to note that any potential negative impact is framed by reference to **the commitments of the EU and international communities, including developing countries, to promote *sustainable* development** – not just any kind of economic development. Therefore – even if indirectly – incentivising unsustainable practices, which may also be **illegal** according to legislation in developing countries, and/or **go against international commitments** of the Union and third countries,[57] is neither in the interest of the Union nor of the developing countries. It can be expected that most cases where de-risking will result in disengagement with suppliers and abandoning certain activities will concern illegitimate or illegal business practices, or other risks and impacts which cannot be mitigated by a company by any other means.

4.11. Contribution of potential soft mitigation measures

While the proposal itself already includes safeguards against unintended consequences, **focused accompanying measures can improve the effectiveness of implementation**. Companies may rely on **industry schemes and multi-stakeholder initiatives** to support the implementation of their obligation. The Commission and the Member States may facilitate the dissemination of information on such schemes or initiatives and their outcome.

[57] e.g. ILO declaration on fundamental rights at work, bill of human rights, SDGs

In particular, **support provided by Member States and the EU to public authorities and companies in the framework of development cooperation** can foster the creation of a stronger regulatory environment in third countries, thereby helping tackle the root causes of systemic issues. It can also help compliance of third-country companies, by building capacity on the ground, where most needed. For instance, the new Neighbourhood, Development and International Cooperation Instrument[58] and relevant Team Europe initiatives[59] in third countries can provide support to governments for aligning their legislation and enforcement with international labour standards, and can provide specific support for suppliers in third countries to adhere to sustainability standards in their own operations and to exercise due diligence in their value chains.

A comprehensive mapping of existing EU-funded actions that support public authorities and companies in partner countries to build capacities in addressing a wide range of human rights and environment-related impacts identified about 75 relevant Commission actions. These are on-going and have a combined funding volume of approximately EUR 660 million, the majority of which being funded through EU development cooperation instruments. Moreover, in the programming of EU development cooperation instruments for the 2021-2027 Multiannual Financial Framework, about two thirds of partner countries identified supply chain sustainability among the objectives or results of proposed priority areas for their development cooperation with the Union.

4.12. Impact on competition

The Board's opinion also pointed to the need to assess the impacts on competition that may arise from potentially increased vertical integration or from the exchange of commercially sensitive information resulting from joint company value chain due diligence efforts.

In the Commission's assessment, **cooperation on due diligence pursuing a sustainability objective** or the **exchange of information limited to what is necessary** for this purpose as such is **unlikely to raise concerns of anti-competitive behaviou**r. This is **being clarified in the ongoing revision of the two Horizontal (Research & Development and Specialisation) Block Exemption Regulations and the accompanying Horizontal Guidelines** which have a dedicated chapter on sustainability agreements, possibly relevant in the context of joint industry efforts whereby companies pool their resources to assess suppliers and vet those that do not meet the required sustainability standards. The guidelines will contain a safe-harbour for sustainability standards, based on procedural conditions (voluntary and non-discriminative participation for companies, transparency, proper mechanism for vetting suppliers etc.).

In the same vein, **it is unlikely that mandatory due diligence will result in anti-competitive behaviour as a result of potentially increased vertical integration**. **In sectors with limited number of suppliers, it is also unlikely that companies will**

[58]https://ec.europa.eu/info/funding-tenders/find-funding/eu-funding-programmes/global-europe-neighbourhood-development-and-international-cooperation-instrument_en
[59] https://europa.eu/capacity4dev/wbt-team-europe

attempt to acquire them – leaving their competitors without available independent suppliers to source from – directly as a result of mandatory due diligence rules because it remains a relatively costly course of action. Literature on the topic[60] suggests that firms are more likely to increase the supply chain risk management activities, which implies in particular **stronger communication and monitoring activities** both upstream and downstream. The same literature suggests a positive association of increased supply chain risk management with all forms of supply chain integration; however, in those increases of supply chain integration, supplier integration is shown to be much less effective compared to **increased control within firms and groups of firms** (i.e. within existing corporate legal entities); similarly, **the increase of customer integration can be expected to be weak** as well, hence the risk of anti-competitive effect is lower. In addition, **EU merger control rules**, that are triggered once companies realise a certain turnover on the Union market, will limit the risks of anticompetitive vertical integration that may lead to input foreclosure or customer foreclosure. Similarly, **third countries' merger control rules** (most of the countries in the world have a modern merger control regime) should address at least part of these risks.

As a result, while there will always be individual cases where supplier integration will reduce the availability of suppliers to other companies (and this could very well be a strategic motive of the acquisition of the supplier to begin with), the empirical literature surveyed does **not suggest that stronger due diligence requirements by themselves (and the related costs) would be a sufficient/material incentive for the acquisition** of a strategic supplier; both the acquiring and the acquired firm risk **losing specialization gains** and risk **increase in complexity**[61].

On the other hand, **vertical integration by EU companies**, be it by form of acquisition compliant with competition rules or by a decision to start supplying a certain input internally, **may contribute to EU companies gaining market share**, or deciding to **invest more** to allow for the development of new products and sustainable technologies and **fostering competition in sustainable products and services**, in line with the market demand.

4.13. Impact on competitiveness

The Board's opinion recommended to assess in more detail the impact the initiative will have on the competitiveness of EU companies, especially when companies have less

[60] Cigdem Ataseven, Anand Nair, Assessment of supply chain integration and performance relationships: A meta-analytic investigation of the literature, International Journal of Production Economics, Volume 185, 2017, Pages 252-265, and Manal Munir, Muhammad Shakeel Sadiq Jajja, Kamran Ali Chatha, Sami Farooq, Supply chain risk management and operational performance: The enabling role of supply chain integration, International Journal of Production Economics, Volume 227, 2020.

[61] For example, in terms of information system requirements external integration remains challenging: as Ataseven et al (2017), surveying the supply chain integration literature up to 2017 note (on page 262), "(...) [i]nternal integration should generally precede external integration since it is important for the processes within an organization to be aligned before engaging in information sharing and collaboration activities with external supply chain partners."

possibility to diversify their suppliers, and the impact on companies' innovation capacity, dynamism and agility, also in the context of possible increase of litigation.

This initiative has been designed so as **to limit the possible negative impacts on EU competitiveness to minimum**, including by designing **clear criteria for civil liability** and linking it to **more stringent** conditions when it comes to value chain relationships beyond first-tier suppliers, by providing **supporting measures** within the Union and in producing countries outside the Union, and by making **disengagement only as last resort requirement and only for severe adverse impacts**. The **dynamic** character of due diligence processes may prove as an additional tool for companies **to diversify suppliers, where available, or actively engage with existing suppliers** to mitigate adverse impacts. Abandoning certain high-risk suppliers could result in European companies **paying higher prices** if sourcing possibilities become more limited or more expensive than those available to non-European suppliers. By covering third-country company competitors, **this risk is also reduced**.

While the **initial cost** of setting up due diligence will affect companies to certain extent, given their size and economic capacity, and the fact that **under the revised scope** all of the companies covered are already subject to non-financial reporting obligations or will be covered by the new sustainability reporting rules, it is likely that **they have or will have, at least partially, some relevant processes already in place**, as regards for instance impact identification and analysis.

These large companies are **likely to be able to absorb the initial costs** of establishing – or topping up existing – processes more easily. They are also more likely to be able **to bear the one-off transition costs**, i.e. to invest in the sustainability transition of the company, and **then reap the benefits of this**, in particular in the medium to longer run.

Annex 4 of the impact assessment provides a list of available evidence on how companies can benefit from improving their sustainability performance and specifically from implementing sustainable corporate governance practices (including due diligence). While risk management will not be specifically required under the revised preferred option, the risk identification duty and due diligence will still provide important data for corporate risk management, which will help the company manage its own sustainability risks, too, including its dependencies on its employees, suppliers, stakeholders, and on natural resources. The impact identification and assessment process, as well as engagement with business partners, can also point to opportunities for the company. Evidence listed in the impact assessment clearly shows that benefits do not only arise in the form of improved external impacts but also in the form of **concrete financial benefits for the company itself**, via numerous possible channels that increase revenue or decrease costs.

One of the sources of improved financial performance of companies with sustainable corporate governance practices is **sustainability-linked product and process innovation**. As the impact assessment explains, this initiative has a strong potential to lead to innovation benefits, which is also backed by the growing demand for sustainable products, technologies, processes, and investment opportunities, and because

sustainability will most likely determine, as a factor, the success and profitability of companies in the long term. The initiative, including the specific due diligence requirements, directors' duties and duty of care, **have been designed so as to spur investment** for the benefit of the long-term sustainable development of the company.

It should be also stressed that by abandoning/limiting commercial relationships that include risks of flagrant violation of human rights (e.g. forced labour, worst forms of child labour), when such risks cannot be mitigated, **companies reduce their legal risks (most of these practices are illegal) as well as their reputational risks** (e.g. customers may boycott products issued from forced labour) and respond to the expectations of their customers and of society as large. In fact, not curbing such practices that are often illegal (child labour, forced labour), but still pursed by some companies, introduces **moral hazard** opportunities and **distorts the level playing field** for the companies who respect their obligations. When taking an overall picture, **an alleged competitive advantage built not on the merits, but on exploitation and against European values does not seem very durable** and is **not something the Union as a society, including both the private and public sector, should pursue**. This proposal may contribute to **enhance the resilience and competitiveness** of EU companies by ensuring that also throughout the value chain, they control better their risks and they offer more sustainable products. The Commission will nonetheless closely monitor the impact of this legislation on companies and other affected stakeholders.

As explained in the impact assessment[62], the above-mentioned considerations that companies can reduce their risk of litigation by conducting due diligence properly seems to be supported by the actual experience with the French law, which shows that the law **did not lead to an increased number of litigation** and thus the potential negative impact on competitiveness has not materialized. In addition, in the proposal the civil liability is based on clear conditions, and includes stricter conditions for liability beyond direct value chain business relationships.

Even if there remains a certain degree of uncertainty that all the benefits mentioned in the impact assessment or in this document would materialize, and the extent to which they arise will not be the same for all companies, the above considerations suggest that the **benefits** of the requirements of this initiative **are expected to outweigh its costs even at the corporate level, and will bring competitive advantages, at least in the medium to long-term.**

[62] Please refer to the annexes of the impact assessment report, p. 63.

Annex 1

List of human rights and environmental due diligence obligations

1. Violations of rights and prohibitions included in international human rights agreements

1. Violation of the people's right to dispose of a land's natural resources and to not be deprived of means of subsistence in accordance with Article 1 of the International Covenant on Civil and Political Rights;
2. Violation of the right to life and security in accordance with Article 3 of the Universal Declaration on Human rights;
3. Violation of the prohibition of torture, cruel, inhuman or degrading treatment in accordance with Article 5 of the Universal Declaration of Human Rights;
4. Violation of the right to liberty and security in accordance with Article 9 of the Universal Declaration of Human Rights;
5. Violation of the prohibition of arbitrary or unlawful interference with person's privacy, family, home or correspondence and attacks on their reputation, in accordance with Article 17 of the Universal Declaration of Human Rights;
6. Violation of the prohibition of interference with the freedom of thought, conscience and religion in accordance with Article 18 of the Universal Declaration of Human Rights;
7. Violation of the right to enjoy just and favourable conditions of work including a fair wage, a decent living, safe and healthy working conditions and reasonable limitation of working hours in accordance with Article 7 of the International Covenant on Economic, Social and Cultural Rights;
8. Violation of the prohibition to restrict workers' access to adequate housing, if the workforce is housed in accommodation provided by the company, and to restrict workers' access to adequate food, clothing, and water and sanitation in the work place, in accordance with Article 11 of the International Covenant on Economic, Social and Cultural Rights;
9. Violation of the right of the child to have his or her best interests given primary consideration in all decisions and actions that affect children in accordance with Article 3 of the UN Convention of the Rights of the Child; violation of the right of the child to develop to his or her full potential in accordance with Article 6 of the UN Convention of the Rights of the Child; violation of the right of the child to the highest attainable standard of health in accordance with Article 24 of the UN Convention on the Rights of the Child, violation of the right to social security and an adequate standards of living in accordance with Article 26 and 27 of the UN Convention on the Rights of the Child; violation of the right to education in accordance with Article 28 of the UN Convention on the Rights of the Child; violation of the right of the child to be protected from all forms of sexual exploitation and sexual abuse and, and to be protected from being abducted, sold or

moved illegally to a different place in or outside their country for the purpose of exploitation, in accordance with Articles 34 and 35 of the UN Convention of the Rights of the Child;

10. Violation of the prohibition of the employment of a child under the age at which compulsory schooling ends according to the law of the place of employment, provided that the age of employment is not less than 15 years, except where the law of the place of employment so provides in accordance with Article 2 (4) and Articles 4 to 8 of Convention No. 138 of the International Labour Organization of 26 June 1973 concerning Minimum Age for Admission to Employment;

11. Violation of the prohibition of the worst forms of child labour for children under 18 years of age; in accordance with Article 3 of Convention No. 182 of the International Labour Organization of 17 June 1999 concerning the Prohibition and Immediate Action for the Elimination of the Worst Forms of Child Labour. This includes:

    a) All forms of slavery or practices similar to slavery, such as the sale and trafficking of children, debt bondage and serfdom, as well as forced or compulsory labour, including the forced or compulsory recruitment of children for use in armed conflicts,
    b) The use, procuring or offering of a child for prostitution, for the production of pornography or for pornographic performances,
    c) The use, procuring or offering of a child for illicit activities, in particular for the production of or trafficking in drugs,
    d) Work which, by its nature or the circumstances in which it is carried out, is likely to harm the health, safety or morals of children;

12. Violation of the prohibition of forced labour; this includes all work or service that is exacted from any person under the menace of any penalty and for which the said person has not offered himself or herself voluntarily, for example as a result of debt bondage or trafficking in human beings; excluded from forced labour are any work or services that comply with Article 2 (2) of ILO Forced Labour Convention, 1930 (No. 29) concerning Forced or Compulsory Labour or with Article 8 (3) (b) and (c) of the International Covenant on Civil and Political Rights;

13. Violation of the prohibition of all forms of slavery, practices akin to slavery, serfdom or other forms of domination or oppression in the workplace, such as extreme economic or sexual exploitation and humiliation in accordance with Article 4 of the Universal Declaration of Human Rights, Art. 8 of the International Covenant on Civil and Political Rights;

14. Violation of the prohibition of human trafficking in accordance with Article 3 of the Palermo Protocol to Prevent, Suppress and Punish Trafficking in Persons Especially Women and Children, supplementing the United Nations Convention against Transnational Organized Crime;

15. Violation of the prohibition of disregarding the freedom of assembly and association in accordance with Article 20 of the Universal Declaration of Human

Rights, Articles 21 and 22 of the International Covenant on Civil and Political Rights and Article 8 of the International Covenant on Economic, Social and Cultural Rights, ILO-Convention No. 87 concerning Freedom of Association and Protection of the Right to Organise, ILO-Convention No. 98 concerning the right to organise and Collective Bargaining, including the following rights:

a) workers are free to form or join trade unions,
b) the formation, joining and membership of a trade union must not be used as a reason for unjustified discrimination or retaliation,
c) workers' organisations are free to operate in accordance with applicable in line with their constitutions and rules without interference from the authorities;
d) the right to strike and the right to collective bargaining;

16. Violation of the prohibition of unequal treatment in employment, unless this is justified by the requirements of the employment; unequal treatment includes, in particular, the payment of unequal remuneration for work of equal value;

17. Violation of the prohibition of withholding an adequate living wage in accordance with Article 7 of the International Covenant on Economic, Social and Cultural Rights;

18. Violation of the prohibition of causing any measurable environmental degradation, such as harmful soil change, water or air pollution, harmful emissions or excessive water consumption or other impact on natural resources, that

a) impairs the natural bases for the preservation and production of food or
b) denies a person access to safe and clean drinking water or
c) makes it difficult for a person to access sanitary facilities or destroys them or
d) harms the health, safety, the normal use of property or land or the normal conduct of economic activity of a person or
e) affects ecological integrity, such as deforestation,

in accordance with Article 3 of the Universal Declaration of Human Rights, Article 5 of the International Covenant on Civil and Political Rights, Article 12 of the International Covenant on Economic, Social and Cultural Rights;

19. Violation of the prohibition to unlawfully evict or take land, forests and waters when acquiring, developing or otherwise use land, forests and waters, including by deforestation, the use of which secures the livelihood of a person in accordance with Article 11 of the International Covenant on Economic, Social and Cultural Rights;

20. Violation of the indigenous peoples' right to the lands, territories and resources which they have traditionally owned, occupied or otherwise used or acquired based on Article 25, 26 (1) and (2), 27, and 29 (2) of the United Nations Declaration on the Rights of Indigenous Peoples;

21. Violation of a prohibition not covered by points 1 to 20 above but included in the human rights agreements listed in Section B of this Part, which directly impairs a legal interest protected in those agreements, provided that the company concerned could have reasonably established the risk of such impairment and any appropriate

measures to be taken in order to comply with the obligations referred to in Article 4 of this Directive taking into account all relevant circumstances of their operations, such as the sector and operational context.

2. Human rights and fundamental freedoms conventions

- The Universal Declaration of Human Rights;
- The International Covenant on Civil and Political Rights;
- The International Covenant on Economic, Social and Cultural Rights;
- The Convention on the Prevention and Punishment of the Crime of Genocide;
- The Convention against Torture and other Cruel, Inhuman or Degrading Treatment or Punishment;
- The International Convention on the Elimination of All Forms of Racial Discrimination;
- The Convention on the Elimination of All Forms of Discrimination against Women;
- The Convention on the Rights of the Child;
- The Convention on the Rights of Persons with Disabilities;
- The United Nations Declaration on the Rights of Indigenous Peoples;
- The Declaration on the Rights of Persons Belonging to National or Ethnic, Religious and Linguistic Minorities;
- United Nations Convention against Transnational Organised Crime 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;
- The International Labour Organization's Declaration on Fundamental Principles and Rights at Work;
- The International Labour Organization's Tripartite declaration of principles concerning multinational enterprises and social policy;
- The International Labour Organization's core/fundamental conventions:
    - Freedom of Association and Protection of the Right to Organise Convention, 1948 (No. 87)
    - Right to Organise and Collective Bargaining Convention, 1949 (No. 98)
    - Forced Labour Convention, 1930 (No. 29) and its 2014 Protocol;
    - Abolition of Forced Labour Convention, 1957 (No. 105)
    - Minimum Age Convention, 1973 (No. 138)
    - Worst Forms of Child Labour Convention, 1999 (No. 182)
    - Equal Remuneration Convention, 1951 (No. 100)
    - Discrimination (Employment and Occupation) Convention, 1958 (No. 111)

PART II

VIOLATION OF INTERNATIONALLY RECOGNIZED OBJECTIVES AND PROHIBITIONS INCLUDED IN ENVIRONMENTAL CONVENTIONS

1. Violation of the obligation to take the necessary measures related to the use of biological resources in order to avoid or minimize adverse impacts on biological diversity, in line with Article 10 (b) of the 1992 Convention on Biological Diversity, [and taking into account possible amendments following the post 2020 UN Convention on Biological Diversity]], including the obligations of the Cartagena Protocol on the development, handling, transport, use, transfer and release of living modified organisms and of the Nagoya Protocol on Access to Genetic Resources and the Fair and Equitable Sharing of Benefits Arising from their Utilization to the Convention on Biological Diversity of 12 October 2014;
2. Violation of the prohibition to import or export any specimen included in an Appendix of the Convention on International Trade in Endangered Species of Wild Fauna and Flora (CITES) of 3 March 1973 without a permit, pursuant to Articles III, IV and V.
3. Violation of the prohibition of the manufacture of mercury-added products pursuant to Article 4 (1) and Annex A Part I of the Minamata Convention on Mercury of 10 October 2013 (Minamata Convention);
4. Violation of the prohibition of the use of mercury and mercury compounds in manufacturing processes within the meaning of Article 5 (2) and Annex B Part I of the Minamata Convention from the phase-out date specified in the Convention for the respective products and processes;
5. Violation of the prohibition of the treatment of mercury waste contrary to the provisions of Article 11 (3) of the Minamata Convention;
6. Violation of the prohibition of the production and use of chemicals pursuant to Article 3 (1) (a) and Annex A of the Stockholm Convention of 23 May 2001 on Persistent Organic Pollutants (POPs Convention), in the version of Regulation (EU) 2019/1021 of the European Parliament and of the Council of 20 June 2019 on persistent organic pollutants (OJ L 169 of 26 May 2019 pp. 45-77), as last amended by Commission Delegated Regulation (EU) 2021/277 of 16 December 2020 (OJ L 62 of 23 February pp. 1-3);
7. Violation of the prohibition of the handling, collection, storage and disposal of waste in a manner that is not environmentally sound in accordance with the regulations in force in the applicable jurisdiction under the provisions of Article 6 (1) (d) (i) and (ii) of the POPs Convention;
8. Violation of the prohibition of importing those of the chemicals listed in Annex III of the Convention on the Prior Informed Consent Procedure for Certain Hazardous Chemicals and Pesticides in International Trade (UNEP/FAO) (The PIC Convention) Rotterdam, 10 September 1998, as indicated by the importing Party to the Convention in line with the Prior Informed Consent (PIC) Procedure;
9. Violation of the prohibition of the production and consumption of specific substances that deplete the ozone layer (i.e., CFCs, Halons, CTC, TCA, BCM, MB, HBFCs and HCFCs) after their phase-out pursuant to the Vienna

Convention for the protection of the Ozone Layer and its Montreal Protocol on substances that deplete the Ozone Layer;

10. Violation of the prohibition of exports of hazardous waste within the meaning of Article 1 (1) and other wastes within the meaning of Article 1 (2) of the Basel Convention on the Control of Transboundary Movements of Hazardous Wastes and their Disposal of 22 March 1989 (Basel Convention), as last amended by the Third Ordinance amending Annexes to the Basel Convention of 22 March 1989 of 6 May 2014, and within the meaning of Regulation (EC) No 1013/2006 of the European Parliament and of the Council of 14 June 2006 on shipments of waste (OJ L 190 of 12 July 2006 pp. 1-98) (Regulation (EC) No 1013/2006), as last amended by Commission Delegated Regulation (EU) 2020/2174 of 19 October 2020 (OJ L 433 of 22 December 2020 pp. 11-19)

    i. to a party that has prohibited the import of such hazardous and other wastes (Article 4 (1) (b) of the Basel Convention),
    ii. to a state of import as defined in Article 2 no. 11 of the Basel Convention that does not consent in writing to the specific import, in the case where that state of import has not prohibited the import of such hazardous wastes (Article 4 (1) (c) of the Basel Convention),
    iii. to a non-party to the Basel Convention (Article 4 (5) of the Basel Convention),
    iv. to a state of import if such hazardous wastes or other wastes are not managed in an environmentally sound manner in that state or elsewhere (Article 4 (8) sentence 1 of the Basel Convention);

11. Violation of the prohibition of the export of hazardous wastes from countries listed in Annex VII to the Basel Convention to countries not listed in Annex VII (Article 4A of the Basel Convention, Article 36 of Regulation (EC) No 1013/2006);

12. Violation of the prohibition of the import of hazardous wastes and other wastes from a non-party to the Basel Convention (Article 4 (5) of the Basel Convention);

Annex 2

Summary of costs and benefits

Annex 3 of the Impact Assessment Report summarised, in a qualitative manner, the benefits of the preferred option for the various stakeholder groups impacted by the initiative. The same annex also gave an overview of the estimated aggregated business compliance costs and costs incurred by public institutions, and it included a qualitative summary of other costs that had not been quantified.

The following two tables present an overview of the expected benefits and costs of the revised preferred option, i.e. taking into account the final content of the Commission's proposal. The tables are presented according to the Better Regulation Guidelines as revised in the meantime, the main implication of which is that administrative costs are now also presented in an additional table to support the implementation of the "One-In-One-Out" principle.

Regarding the benefits, the proposal has been carefully calibrated so that the expected benefits for the company's stakeholders in terms of less human rights violations and environmental harm remain high. At the same time, due to the reduced scope, only a smaller number of companies will directly reap benefits such as those deriving from improved corporate management systems, long-term operational costs savings, new marketing opportunities, or attracting talents. Benefits related to the specific obligation to manage risks – beyond mitigating the adverse corporate impacts in line with the due diligence obligations – will not manifest themselves fully due to the reduced content of the proposal, even though the obligation to identify sustainability risks, together with the duties related to the corporate strategy, has the potential to improve corporate risk management to a similar extent.

The most significant changes in the impacts nevertheless concern the quantified cost elements, due to the reduced scope and content of the initiative (which will now only include due diligence-related cost elements due to the dropping of those directors' duties for which the impact assessment calculated with additional compliance costs). In parallel with this, the non-quantified cost elements, namely the costs of transition to sustainability, the indirect business compliance costs in relation to the corporate due diligence obligation, the costs of other directors' duties, will also be smaller. While some of the companies that are now out of the direct scope will nevertheless incur some indirect costs in relation to due diligence now as value chain partners of larger companies, such indirect costs for SMEs are likely to be smaller now also due to the provisions that specifically address the trickle-down effect in the proposal. Costs for non-EU companies were not quantified in the impact assessment but are now quantified (monetised) and presented separately, and the supervisory costs now include the costs incurred both with regard to EU and non-EU companies' supervision.

As explained in the impact assessment, directors' duties will result in some additional compliance costs for businesses as internal processes and management systems would need to be revised to ensure that directors are able to meet their clarified general duty to

promote the best interest of the company, and their harmonised specific obligations. However, as also explained in the impact assessment the duties that were retained in the proposal are not expected to result in significant cost increases in addition to the (new) due diligence obligation and the public reporting obligation under the CSRD, due to overlaps between the impact and risk identification and between the reporting rules and the substantive duties, as well as due to already existing practices. Accordingly, we will not calculate with additional recurrent costs (the one-off costs elements for risk management and science-based target setting will not arise under the revised preferred option).

As a result of the new rules on directors' remuneration, companies would need to revise their remuneration policies and bear the related adjustment costs. These costs should be very small, in particular for non-listed companies which neither have to publish their remuneration policy nor to report on it. Therefore, compliance and adjustment costs will be minor and could even be regarded as part of business as usual.

I. Overview of Benefits (total for all provisions) – Preferred Option		
Description of benefit	***Which stakeholder group is the recipient of the benefit?***	***Comments***
Direct benefits		
Adverse human rights, health and social impacts are reduced, and value creation by companies becomes more sustainable, responsible and fair.	**Actual and possible victims** of adverse human rights impact of companies, including the **employees** of the company and its **value chain partners**, as well as **local communities** will benefit directly from this. In addition, the **company** itself will also reap benefits directly.	Actual and possible victims will benefit from the reduction of human rights violations as a result of two factors: (1) the **corporate due diligence** obligation includes a specific requirement to **cease or minimise** actual adverse impacts, and also has a requirement to **prevent** potential adverse impacts to the extent possible, (2) improved access to justice for victims of human rights violations via harmonised **civil liability** rules will have a **preventive effect**. The company itself will also benefit from the reduction of its adverse human rights impact directly, including due to **reduced financial risks related to possible litigation**.
Adverse impacts on climate, biodiversity, pollution, and the environment more broadly are reduced, and value creation by companies becomes more sustainable, responsible and "green".	The **environment**, as well as **actual and possible victims** of the environmental harm which companies cause or contribute to, including people and local communities along the company's value chains and the company's other stakeholders, will directly benefit from such an impact. In addition, the **company** itself will also reap benefits directly.	Similarly to human rights impacts, benefits are expected to arise due to both the requirement to stop harmful activities or mitigate actual and potential adverse impacts, and the preventive effect of victims' improved access to remedy. The company itself will also benefit directly, including due to reduced financial risks related to possible litigation.
Access to remedy for victims of human rights violations and of environmental harm **improves**.	**Victims** of human rights violations and of environmental damage, including those that take place in the **value chains** located in the **EU** and in **third**	

I. Overview of Benefits (total for all provisions) – Preferred Option		
Description of benefit	***Which stakeholder group is the recipient of the benefit?***	***Comments***
	countries will directly benefit from this.	
Medium to long-term competitiveness, resilience and viability of the company improves (economic sustainability).	The **company** itself will benefit directly, but all other stakeholders, including owners (shareholders or members), will also benefit (indirectly).	**This beneficial impact** derives from the due diligence obligation as the identification of the actual and possible adverse impacts will directly help companies **know their value chains better**, as a result of which the company can better identify and manage their dependencies and other financial risks they face in relation to sustainability matters. Furthermore, the harm mitigation obligation can also contribute to long-term competitiveness and viability by **catalysing investments into more sustainable and future-proof technologies and into the workforce** etc. Companies with reduced harmful external impacts are also likely to have **competitive benefits as a more sustainable (responsible and green) company in the labour, customer and suppliers markets** (also using the first movers' advantages referred to in the next point). The benefits can materialise already in the **medium term** in the form of **improved financial performance** of the company. Such benefits are also reinforced by the requirement that **directors**, when fulfilling their duty to act in the best interest of the company and taking decisions in their capacity as directors, take into account the human rights, and environmental consequences of those decisions and their likely consequences in the long term, which, among others, involves the proper management of sustainability-related risks and dependencies on natural and human capital.
Better medium to long-term competitiveness in **global markets** (beyond the EU) due to benefitting from **first mover's advantages**.	This will directly benefit the **company**.	As additional company-level costs per revenue remain relatively low, no significant negative distortions for EU exporters are expected. At the same time, EU companies could reap the first movers' competitive advantages. These derive from being able to **grab the opportunities offered by the sustainability transition sooner** than competitors and increasing their market shares in global markets due to growing global demand for sustainable products. Further first-movers benefits include: securing access to resources, technology, gaining economies of scale vis-à-vis competitors that later market entrants, etc.
Indirect benefits		
Sustained financial	The company's **owners**	These benefits derive form the fact that

I. Overview of Benefits (total for all provisions) – Preferred Option		
Description of benefit	***Which stakeholder group is the recipient of the benefit?***	***Comments***
return on investment over a longer time horizon.	(members or shareholders, including financial investors), will directly benefit from this.	**companies with improved financial performance, resilience, competitiveness and viability over the longer run are able to pay** sustained financial returns to their shareholders over the longer run, too.
Sustained **job opportunities**, sustained **demand for suppliers' products and services**, sustained **sourcing opportunities** and continued access to after-sales services for customers etc., problem-free **repayment of loans** (or profitable return on bonds), etc.	In addition to direct positive impacts, **employees, suppliers** (and their employees), **customers**, as well as **creditors** (or bond-holders) are also indirectly benefitting from the new directive. In addition, **local communities**, and the **economy** as a whole will benefit.	This indirect effect is the result of companies' longer term competitiveness, resilience and viability: **companies that remain successful over the medium and long run are likely to continue** employing the workers, purchasing from their suppliers, providing their products and services to their clients, including reparation etc., service their loans (or bond payments), etc. Their sustained **contribution to employment, and participation in the flow of economic activities**, has, in turn, a positive impact on the local communities and the economy as a whole.
Improved resilience, and improved medium to long-term competitiveness of the EU economy	The entire **EU economy** as well as indirectly impacted **third countries** will benefit from this impact.	**The cumulative medium to long-term net benefits for companies** are expected to result in medium to long-term competitiveness gains for the economy. A focus on the long-term interest of the company, better risks management, lower dependency on increasingly scarce natural resources, improved resilience to sustainability-related shocks, as well as impact mitigation will all contribute to this impact.
Better working conditions and **increased environmental standards and respect for human rights**	**Third countries**, in particular **where standards** regarding working conditions and respect by companies for human rights the environment **are lower**, will, in general, benefit indirectly.	
Faster and more systematic **transition to a sustainable**, i.e. green and fair **economy and society**	On the top of direct benefits, the **entire economy and society**, including **current and future generations** of people **in the EU and around the world** will benefit indirectly.	Reduced climate and environmental footprint, better respect for human rights, diminishing adverse health and social impact on workers and other people will contribute to speeding up the transition to a greener and fairer society and economy, and to ensuring better conditions for life for the future generations.
Administrative cost savings related to the 'one in, one out' approach*		
(direct/indirect)	N/A	N/A

II. Overview of costs – Preferred option							
		Citizens / Consumers		**Businesses**		**Administrations**	
		One-off	**Rec.**	**One-off**	**Recurrent**	**One-off**	**Recurrent**
Corporate due diligence	Direct adjustment costs	N/A	N/A	EUR 220 million for EU companies and EUR 70 million for non-EU companies + Cost of transition to sustainability (not quantified, but qualitative and quantitative examples with cost ranges are given in the impact assessment)	EUR 760 million for EU companies and EUR 240 million for non-EU companies No other additional recurrent cost is expected.	N/A	N/A
	Direct administrative costs	N/A	N/A	No substantial additional administrative costs will be incurred by EU companies as all of the companies covered by the scope of the revised preferred option are also under the CSRD proposal, and a such their costs related to reporting and the necessary data collection, data analysis, documentation etc. costs have already been counted as a direct compliance costs under that proposal.		N/A	N/A
	Direct regulatory fees and charges	N/A	N/A	N/A	N/A	N/A	N/A
	Direct enforcement costs	N/A	N/A	N/A	N/A	EUR 0.13 million	EUR 5.55 million
	Indirect costs	N/A	N/A	While part of such indirect costs are included in the qualitative estimations of direct costs (which cover the cost of due diligence through the entire value chain and in subsidiaries), some compliance costs could still **trickle down** to companies (including SMEs) which are not under the scope but belong to the value chain of companies which are themselves covered. The proposal includes safeguards to minimise such impacts on SMEs.		N/A	N/A
Directors' duties	Any direct or indirect costs	N/A	N/A	The costs of directors' duties linked to the corporate due diligence obligations are already included in the cost of due diligence above. Directors or companies will not incur any substantial other additional costs as a result of harmonising other directors' duties: these costs should remain minimal and can even be regarded as part of business as usual.		N/A	N/A

Directors' remuneration	Any direct or indirect costs	N/A	N/A	Costs related to adjustment of existing remuneration policies - and, for listed companies, reporting – have not been quantified but should remain minimal and can even be regarded as part of business as usual.		N/A	N/A
Costs related to the 'one in, one out' approach							
Total	Direct adjustment costs	N/A	N/A	EUR 220 million for EU companies + Cost of transition to sustainability (not quantified)	EUR 760 million for EU companies		
	Indirect adjustment costs	N/A	N/A	Some indirect compliance costs deriving from the trickle-down effect for companies, incl. SMEs, belonging to the value chains of large companies can occur in addition to those already included in the estimated direct costs (not quantified).			
	Admin. costs (for offsetting)	N/A	N/A	No substantial additional administrative costs will be incurred by EU companies under this directive as all of the companies that are under the scope of the revised preferred option are also under the CSRD proposal, and as such their costs related to reporting and the necessary data collection, data analysis, documentation etc. costs have already been counted as a direct compliance costs under that proposal.			

(1) Estimates are provided with respect to the dynamic baseline (including the CSRD proposal);
(2) Aggregated direct costs for companies are likely to be overestimated because of the cautious calculation method of calculating firm-level costs;
(3) One-off costs for companies are not immediate costs and can be spread across several years;

Annex 3

Overview of how the comments of the Regulatory Scrutiny Board have been addressed

This comparison table describes how the four general comments and the 19 specific recommendations for improvements made by the Regulatory Scrutiny Board (RSB) in its second opinion of 26 November 2021 have been addressed in the amended preferred option (forming the basis of the legislative proposal) and in this Staff Working Document (SWD) accompanying the legislative proposal.

General RSB comments (i.e. summary of main findings)	Description of how the general comments of the RSB have been addressed
(1) The problem description remains vague and does not demonstrate the scale and likely evolution of the problems the initiative aims to tackle. It does not 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.	This comment has been addressed by providing additional evidence as regards the problem description in this accompanying document. The following has been added: - evidence on improving sustainable operation of companies but insufficient or slow uptake of value chain due diligence by the majority of companies; - more information on the added value of the initiative with regard to related measures; - more information on the links with international obligations, trade policy and development support measures and impact of trade and development support measures. See more details below under the RSB specific comments No. 1 and 2, notably regarding the problem definition.
(2) The presented policy options remain too limited in scope. Key policy choices are not identified nor fully assessed	The narrative and preferred option put forward by the impact assessment were reviewed following the second opinion from the Board. As a result, **the proposal sets out a more focused and targeted due diligence obligation** for companies. The impact assessment options have not been revised as such for the sake of transparency, but the **initiative is now based on a combination of elements that represents a new preferred option** compared to the impact assessment report. The narrative emphasises – in addition to the contribution of the initiative to the sustainability transition – the need to **address the risk of fragmentation** in the Single Market due to new legal frameworks on due diligence requirements emerging in Member States. **The measures selected for inclusion in the**

General RSB comments (i.e. summary of main findings)	Description of how the general comments of the RSB have been addressed
	proposed legislative text have been significantly reviewed and revised, **leaving out part of the directors' duties and of the rules on directors' remuneration** (apart from the obligation to take into account the emission reduction plan when setting directors' variable remuneration). For more details about directors' duties not retained, please see the response to specific comment No. 3. The legislative proposal now **focuses on external impact mitigation through value chain due diligence** and only covers the general duty of directors to take into account the consequences of their decisions for sustainability matters, including where applicable, the climate, environmental and human rights consequences in the short, medium and long term, and the duty to set up and oversee the due diligence and integrate it into the corporate strategy. The **changes as regards due diligence** are the followings: - first, **it has a reduced personal scope** (i.e. who / which business categories are covered) as compared to the preferred policy option put forward by the impact assessment. In particular, **SMEs** and certain midcaps **have been completely excluded**, and the coverage of high-impact sectors has been shifted to "midcap" companies only (companies with more than 250 employees and more than EUR 40 million net turnover but not exceeding the 500 employee and EUR 150 million net turnover thresholds simultaneously). While the impact assessment presented in its Annex 11 an indicative "maximum" list and two scenarios for more limited lists of possible high-impact sectors for political decision, the now selected option builds on the most limited one. The **high-impact sectors** falling under this proposal **have been limited** to sectors and parts of the value chains that are covered by existing OECD due diligence guidance. The changed approach to define high-impact sectors and the increase of applicable minimum size thresholds result in a decrease of the total number of EU companies in the scope to about 12 000. The choices made to ensure that the proposal is more proportionate to the goals of the initiative (e.g. by excluding SMEs, limiting the number of high impact sectors, aligning

General RSB comments (i.e. summary of main findings)	Description of how the general comments of the RSB have been addressed
	the scope of third country companies covered with the one of EU companies, etc.) is provided in the Explanatory Memorandum. This accompanying document contains in section 3 further detailed explanations on the redesign of the selected options in terms of scope and enforcement. Please see also the follow-up to the Boards specific comments No 3 to 11.
(3) The impacts are not assessed in a sufficiently complete, balanced and neutral way. Uncertainty related to the realisation of benefits is not sufficiently reflected.	Additional assessment and evidence regarding impacts (on competition, competitiveness, impact on third countries) is provided in this accompanying document. Concerning the uncertainty on the realisation of benefits for the companies, it is presented how the design of this initiative makes sure that possible negative impacts on EU competitiveness are limited to the minimum (for instance, by designing clear criteria for liability, by providing supporting measures within EU and in producing countries and by making disengagement from value chain partners only a last resort to be applied and only for severe adverse impacts). For more details on the assessment of additional impacts please see below as regards the Board's specific comments No. 12 to 15.
(4) The report does not sufficiently demonstrate the proportionality of the preferred option.	The preferred option has been amended to make it more proportionate to the goals of the initiative by: (1) excluding all SMEs and shielding them from unfair and disproportionate requirements from their business partners in the scope of the proposal, (2) limiting the number of midcap companies in high impact sectors by reducing the range of high impact sectors and their obligations, (3) aligning the scope of third-country companies covered with the one of EU companies, and (4) providing specific conditions for civil liability for damages at the level of indirect established business relationships. The number of companies was very significantly reduced to about 12 000 EU and an additional approximately 4 000 non-EU companies (this latter figure had not been

General RSB comments (i.e. summary of main findings)	Description of how the general comments of the RSB have been addressed
	estimated in the impact assessment).

Specific RSB comments	How the specific RSB comments have been addressed
(1) The report continues to provide little specific evidence on 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 initiative. While the assessment of benefits provides ample evidence on the competitive, financial and reputational advantages that companies achieve by applying corporate sustainability practices, the report should identify, and substantiate with evidence, the obstacles that may prevent companies from pursuing sustainable corporate management practices. It needs to demonstrate more convincingly why the market and competitive dynamics together with the further evolution of companies' corporate strategies and risk management systems are considered insufficient. Moreover, it needs to substantiate better the assumed causal link between using corporate sustainability tools and their practical effect in tackling the problems	To address this comment additional evidence is presented in this accompanying document (section 2) on why the market and competitive dynamics together with the further evolution of companies' corporate strategies and risk management systems are considered insufficient. As regards the recommendation from the Board to identify, and substantiate with evidence, the obstacles that may prevent companies from pursuing sustainable corporate management practices, the impact assessment report contains ample analysis and specific obstacles such as for example cost, knowledge or limited resources are more likely to arise with respect to SMEs which have now been excluded from the scope, therefore this document does not contain new analysis on this.
(2) The report should present a sufficiently developed and more balanced dynamic baseline scenario that integrates (i) the increasing trend of take up of corporate sustainability practices, (ii) the large number of related measures already adopted and parallel regulatory measures being developed (including sectoral and sustainable product due diligence), (iii) the comprehensive package of measures to promote sustainability under the Green Deal and (iv) the developments expected in third countries with sustainability sub-standards resulting from own commitments as well as substantial EU and international trade and development support measures.	Additional evidence is presented in this accompanying document on: - the description of the dynamic baseline scenario, in particular the increasing trend of take up of corporate sustainability practices, also prompted by transparency requirements by investors and consumers (section 2.1); and on - the possible evolution of the problem within the context of the European Green Deal and other EU due diligence measures alone and in synergy with the proposed initiative (section 2.2).
(3) The report is not clear about why it is necessary to regulate directors' duties on top of due diligence requirements. It should better explain and assess the value- added of regulating directors' duties, considering that the due diligence option already requires risk management and engagement with stakeholders' interests. It should justify why stand-alone options covering directors' duties or due diligence requirements only were not identified and subsequently	The proposal differs from the initial preferred options package in the impact assessment by significantly focusing the directors' duties element to those necessary for the proper implementation of the due diligence. As it is crucial that compliance with the due diligence obligation is integrated in corporate governance, in light of the existing international standards (UNGPs, OECD guidelines), directors' duties linked to due diligence have been maintained. This

Specific RSB comments	How the specific RSB comments have been addressed
compared with the combination options.	**encompasses directors' duties relating to putting in place and overseeing due diligence** processes and measures, including integrating due diligence into all their corporate policies and having in place a due diligence policy. **Directors' duties not retained** – as compared to those put forward as part of the preferred option in the impact assessment – concern - the duty to manage sustainability risks to the company and adopt science based targets, i.e. duty to identify stakeholders' interests, dependencies of the company to such stakeholder interests; - the directors' duty to manage risks to the company related to those stakeholders and related dependencies, set up and oversee the implementation of processes related to management of sustainability risks to the company; - the directors' duty to include the management of sustainability risks to the company in the corporate strategy, mandatory adoption and disclosure of science based targets. In order to fully reflect directors' role in light of the corporate due diligence obligations, the general directors' duty of care for the company which is present in all Member State laws is being clarified to make clear that directors take the consequences of their decisions on sustainability matters into account.
(4) As regards enforcement, the report discards mandatory due diligence policy options that do not include a civil liability regime without providing evidence of their apparent lack of effectiveness. Given that stakeholders consider administrative supervision as the preferred option (and this seems a solution also introduced at Member State levels), the report should better assess and compare all feasible enforcement options, including a stand-alone administrative supervision option. The report should also include more detail on the functioning, efficiency and effectiveness of the envisaged sanction regimes (e.g. withdrawal of products from the market, exclusion from public procurement), in particular with respect to non-complying third country undertakings. It should be clearer on the feasibility and impacts of	As the impact assessment report was not revised, no new options have been assessed. However, to address this observation made by the Board, additional evidence is presented in this accompanying document on the enforcement mechanism, in particular further expanding on the added value of a two-pillar enforcement system building on administrative enforcement and civil liability, also in light with what is done with other areas of Union law. As regards the selected option on civil liability, the legislative proposal clarifies that civil liability concerns only established business relationships which are expected to be lasting, in view of their intensity or duration non negligible or non-ancillary character and applies only where the adverse impact could have been identified, prevented, mitigated,

Specific RSB comments	How the specific RSB comments have been addressed
possible overriding mandatory provisions as regards applicable law and assess any unintended consequences.	brought to an end or its extent minimised with appropriate due diligence measures. As it will in practice be difficult to prevent all risks through global value chains, liability is limited to harm done in the value chain under specific conditions beyond direct suppliers. As regards administrative sanctions, the legislative proposal with recitals and explanatory memorandum contains comprehensive details as regards such sanctions and their functioning. As regards international private law elements, in particular as regards applicable law, the legislative proposal provides details as to the content of the selected solution for overcoming problems linked to applicable law. Explanation is contained in the Explanatory Memorandum and this accompanying document
(5) The options extending the scope into medium-sized companies should better account for the results of the new SME study, which shows both a significant uptake already in exposed sectors as well as an important trickle-down effect through the value chain of measures adopted for large companies. The report should better justify and substantiate with evidence why certain medium-sized companies operating in 'high-impact' sectors should be included in the personal scope. It should present clear and objective criteria that would be used in determining such sectors. To the extent that specifying the selection design comes with policy choices (including on the legislative technique to be used, as implementing legislation is mentioned in the annex), these should be assessed and compared in terms of costs and benefits. The report needs to be clearer on the envisaged phasing in of the requirements for medium-sized companies. It should also be more specific on the safeguards it would include to prevent that large companies impose unjustified compliance burden on SMEs in their value chain. If this comes with policy choices, it should present and analyse alternatives.	As already explained with regard to the Board's general comment No. 2 (i.e. coverage of business categories), the personal scope of the selected option has been considerably reduced. SMEs and smaller midcap companies have been fully excluded. Also, a new approach has been adopted to define "high-impact sectors". Annex 11 of the impact assessment proposed an indicative "maximum" list of high-impact sectors covering almost 50 000 companies (in option 3b) and several alternative or more limited approaches to determine the list for a political decision. From among these approaches, the now selected option builds on the most limited one and is based now mainly on the relevant OECD guidance for companies.. The phase-in period for those companies in high-impact sectors has been set at 2 years and the expected benefits have been explained. As regards the trickle-down effect on SMEs in value chains as referred to by the Board, the proposal itself will contain such safeguards (e.g. duty to provide targeted support if necessary, fair and proportionate treatment of SME business partner, contractual clauses, supporting measures) and the Explanatory Memorandum provides details on other support to be given to companies by Member States, in particular to prepare for those effects. Additional support will be provided through development projects in producing countries.

Specific RSB comments	How the specific RSB comments have been addressed
(6) To ensure greater regulatory coherence, the report should consider aligning the personal scope better with the scope of parallel initiatives, such as the Corporate Sustainability Reporting Directive. It should also discuss more thoroughly how coherence will be ensured with the parallel sectoral and product due diligence initiatives and whether these could become (partially) superfluous.	When having recalibrated the preferred option, the personal scope (i.e. coverage of business categories) has been better aligned with the proposed Corporate Sustainability Reporting Directive (CSRD) while ensuring proportionality. Therefore, while a larger number of companies will be subject to reporting obligations under the CSRD, only those companies having a certain capacity and economic power will have a material due diligence duty. The CSRD proposal does not cover the third-country companies. Therefore, full alignment with the scope of CSRD is not achieved, i.e. for instance this directive will not cover listed SMEs (as the new preferred option excludes all SMEs). However, the legal text envisages an implementation report, to be provided 7 years after the transposition period, opening the possibility to further extend and align the scope, if necessary.
(7) The report should be more precise which selected international environmental conventions should be included in the material scope of the due diligence obligations and why. It should ensure that it does not unduly extend specific EU commitments (e.g. from the Climate Law) to third countries.	The legislative proposal and the explanatory memorandum specify and explain which violations based on environmental conventions are included in the retained policy choice (for example Minamata Convention on mercury, Stockholm convention on persistent organic pollutants, etc.). Only those environmental conventions were retained that can be translated into clear obligations for businesses. As regards climate change, companies are required to 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. This plan shall, in particular, identify, on the basis of information reasonably available to the company, the extent to which climate change is a risk for, or an impact of, the company's operations. The review clause explicitly provides for an assessment on whether the Directive should be reviewed to include climate change in due diligence.
(8) Regarding the inclusion of companies without an EU establishment, the report should specify and justify what the 'adequate turnover' threshold should be (the annex mentions EUR 350 million) or assess alternative options in case the Commission enjoys discretion on this. It should make an effort to estimate how many	The net turnover threshold for third-country companies covered by the scope has been specified in the legislative proposal (net turnover of at least EUR 150 million in the EU) to reflect the criteria of EU companies in the scope while not discriminating the non-EU companies. Third-country companies with a turnover of EUR 40 to 150 million that are

Specific RSB comments	How the specific RSB comments have been addressed
foreign companies would be affected respectively, as this is important to assess the proportionality of the measures in terms of overall benefits and costs. It should clarify whether all worldwide activities of foreign companies would be subject to the due diligence duty or only activities with a clear (turnover) link to the EU. Similarly, for companies established in the EU, the report should clarify whether all their global activities under control would be covered (e.g. products produced in China and sold exclusively in the US).	operating in high-impact sectors are also now covered, with the same obligations and phase in as EU companies of a corresponding size. The relevant criteria are being explained in the Explanatory Memorandum and the employee criterion was not retained as it would make it difficult to identify such companies. This accompanying document contains more explanations of applicability and estimations as regards the number of third-country companies covered.
(9) The description of the directors' duties should clarify how directors need to incorporate conflicting interests of stakeholders and sustainability aspects. It should clarify whether or not there is a long-term interest of the company that could supersede particular interests of stakeholders or beneficiaries or particular sustainability considerations.	As specified in response to the Board's specific comment No. 3, and as opposed to the preferred package put forward in the impact assessment, the proposal significantly reduces the directors' duties element by linking it only to the due diligence duty. A number of specific directors' duties that were included in the initial preferred option, has been removed (for a list of the removed directors' duties please see above follow to specific RSB comment No. 3). In the same vein, the clarification of the directors' duty of care for the company as present in Member States laws has been limited to making clear that directors take into account the consequences of their decisions on sustainability matters, including, where applicable, human rights, climate change and environmental consequences, including in the short, medium and long term.
(10) The report should justify and substantiate with evidence the need for a mandatory science based target for climate change mitigation (and potentially also for biodiversity) as part of the corporate strategy of very large companies. It should clarify which gap in climate mitigation legislation it would fill. It should explain how these targets would be established and function and how independent validation would be ensured. It should justify why the requirement for science-based targets is linked to the size of a company and not to the scale of emissions it is responsible for. The report should explain why science based target setting is part of directors' duties and not due diligence, which already requires companies to mitigate adverse effects.	The focus of the selected option has been readjusted compared to the one put forward by the impact assessment. As described above, mandatory science based targets are no longer part of the chosen policy mix. As explained in specific comment No. 7, due to a lack of clear obligations for companies climate change was excluded from due diligence obligations. Instead, the largest companies need to 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.
(11) The report should better explain the precise role of public authorities in checking	Detailed provisions on the role and powers of supervisory authorities are put forward in the

Specific RSB comments	How the specific RSB comments have been addressed
the corporate strategy and the scientific targets. It should also better explain which national authority would be best placed to act with respect to non-compliance of third-country undertakings. It should also explain how effective coordination among national authorities would be ensured, for instance launching ex-officio procedures or imposing sanctions and what role a 'mechanism of EU cooperation/coordination' would play.	legislative proposal, including which supervisor is to act with respect to third country companies. Article 18 lays down in detail supervisory authorities' powers, including as regards powers to carry out investigations and checks on companies, Concerning the supervision of third-country companies, Member States are free to designate the national authority they consider that it has more relevant experience to carry out the tasks set out in the proposal. Article 21 stipulates the framework for a European Network of Supervisory Authorities, including the possibility to coordinate within this network in case of doubts which supervisory authority is competent to carry out investigations or impose administrative sanctions vis-à-vis third country companies. Comprehensive explanations are provided in the recitals and the Explanatory Memorandum.
(12) The report should be more balanced and complete in terms of presenting potential impacts concerning competition, innovation, agility and litigation risks. While stricter sustainability requirements may spur innovation, there is also a risk that due diligence will make companies less dynamic and agile – and more dependent on a set of fixed providers, in particular in highly concentrated sectors, with only a very limited number of suppliers. The report should assess to what extent the measures envisaged will make it more difficult for certain industry sectors to diversify their suppliers and to improve the resilience of their supply chain. It should assess impacts on competition that may arise from potential increased vertical integration by businesses as well as from the exchange of commercially sensitive information resulting from joint company value chain due diligence efforts. It should assess more thoroughly whether the potentially increased risk of (unsuccessful) litigation could also make EU companies less dynamic and agile.	This accompanying document provides more explanations as regards the expected impacts of the proposed intervention on competition and competitiveness (sections 4.5 and 4.6). In particular, explanations are provided to dispel concerns that the proposed measures would lead to anti-competitive behaviour, as a result of cooperation on due diligence pursuing a sustainability objective or the exchange of information, or as a result of vertical integration. As explained under point 3 of the general RSB comments, impacts on competitiveness were further assessed taking into account possible dependencies of EU companies and the risk of litigations, as well as possible impacts on companies' innovation capacity. While there is certain degree of uncertainty about the materialization of all benefits projected in the impact assessment for EU companies, the design of this initiative is such to reduce the possibly negative ones to the minimum. This document includes an explanation about what safeguards have been used in the proposal to make sure that companies continue engaging with suppliers while mitigating adverse impacts, instead of disengagement and diversification of suppliers.
(13) The report should better account for potential negative impacts in third countries, notably in developing countries,	The details about the risks relating to unintended impacts on third countries are presented in this accompanying document

Specific RSB comments	How the specific RSB comments have been addressed
by being more realistic on risks and costs and the contribution of potential soft mitigation measures. It should better assess the risk of 'sustainability leakage'. If EU companies will ultimately have to withdraw from certain suppliers due to sustainability issues, third-country companies (if out of the personal scope) could take over these suppliers and thereby gain a competitive advantage and supply chain control, while leaving no improvement in overall human rights and environmental performance.	(section 4.3), as well as the safeguards in the proposal against such impacts. Such safeguards include: (1) measures ensuring that the emphasis is on preventing and mitigating adverse impacts, rather than banning certain products originating from certain areas, (2) prevention and mitigation should include proper investments, where necessary, (3) prevention and mitigation should include targeted financial or other support for the SME trading partner, where necessary. (4) collaboration with other entities, including, where relevant, to increase the company's ability to bring the adverse impact to an end (5) termination of the business relationship only if the potential adverse impact is severe, and where the law governing their relations so entitles companies to do so. Collaborative efforts will also be fostered through support measures. Those third countries that are main EU trading partners and where the standards linked to sustainability are generally lower will be impacted the most by this initiative. Sustainability leakage is present in few industry sectors but doesn't seem to be a widespread practice so far. As explained, the safeguards aim to ensure continuous engagement and disengagement is only likely for severe adverse impacts such as in case of State imposed forced labour .
(14) Based on a clarification of the personal scope, the report should assess more thoroughly the impacts of the options on the global level playing field and competitiveness of EU companies, in particular for SMEs in scope. While a large number of EU SMEs active in 'high impact' sectors would be covered (e.g. turnover higher than EUR 8 million), this is not the case for their 'SME competitors' established in (neighbouring) third countries (as they are very unlikely to be above the indicated much higher EU turnover threshold of EUR 350 million). The report needs to assess the potential competitive disadvantage for the affected EU SMEs. Similarly, as directors' duties obligations would apply only to EU established companies, the report should assess more thoroughly the impacts on their	As explained in reaction to the Board's general comment No. 1 and specific comment No. 5, SMEs are no longer covered by due diligence obligations under the new policy mix underlying the proposal. The concerns raised by the Board would therefore not arise in this new scenario. As regards directors' duties, as explained, these have also been reduced in the proposal, linking them to due diligence. This implies that the two items that were explained in the impact assessment (section 6.2.1.3) to possibly raise one-off costs for a limited number of companies (EUR 5 000 for the risk management system and EUR 5 000 for the external validation of science based targets) have not been retained now for the legislative proposal put forward.

Specific RSB comments	How the specific RSB comments have been addressed
competitiveness, including the risk that EU companies may relocate their headquarters to (neighbouring) third countries.	
(15) The report should assess how the proposed EU corporate sustainability governance rules would fit with the different national corporate governance models existing in the EU, given the national focus of company law.	Explanations as to how the proposed rules fit with the different national corporate governance models have been provided in the Explanatory Memorandum. Overall, as company law is to a large extent harmonised already, corporate governance models are gradually converging.
(16) While the report provides greater clarity on the substantial costs of the initiative, it still does not sufficiently reflect the high uncertainty that the estimated benefits will actually materialise on a scale to outweigh the costs. The report should therefore further improve the proportionality assessment of the (preferred) option(s) by reconsidering the arguments for the inclusion of medium-sized EU companies operating in high impact sectors and the broad scope of mandatory measures.	As explained above, the personal scope of the initial preferred option was considerably reviewed (exclusion of SMEs and smaller midcaps, reducing the number of high-impact sectors) particularly to improve further the proportionality, based on the additional evidence and considerations following the Board's second opinion. The material scope of the revised preferred option is also more focused on the due diligence obligation of companies, while directors' duties were significantly reduced (keeping only those that are linked to the corporate due diligence obligation). In addition, this accompanying document includes more assessment of the impact on firm-level competitiveness. This shows that as a consequence of including only larger companies in the scope, it is more likely under the revised preferred option all companies will be able to bear the initial costs and also enjoy the benefits of sustainable corporate governance practices, which are expected to outweigh the costs even at the company's level, in particular in the medium or long run.
(17) The comparison of options in terms of effectiveness should analyse the expected achievement of the specific objectives identified in the objectives section.	The comment of the Board concerns the quality of the impact assessment. It was decided to provide utmost transparency and publish the initial impact assessment report without changes. However, additional evidence and explanations are presented in this accompanying document.
(18) The report should present more systematically the views of different stakeholder categories. It should find a better balance between supportive and critical views expressed. The views of SMEs should be singled out to support the discussion on scope and options.	This comment of the Board mainly concerns the quality of the impact assessment. The presentation of the consultation results in the Explanatory Memorandum has been reviewed by adding the SME views. Overall, the views of SMEs and SME associations as collected in the consultative activities correspond largely to overall companies' views.

Specific RSB comments	How the specific RSB comments have been addressed
	It is recalled that SMEs have been excluded from the options.
(19) The report would benefit from a more precise summary of the final preferred option, including in terms of the variation in scope across elements.	This comment of the Board concerns the quality of the impact assessment. As it has been decided, to provide utmost transparency, and not to revise the Impact Assessment Report, the proposed changes to the presentation of the impact assessment could therefore not been made. The initial preferred option has been revised, as explained above, and additional explanations provided in this accompanying document and the Explanatory Memorandum.