

## European Commission Publishes Proposed Law Requiring Value Chain Human Rights and Environmental Due Diligence

07 March 2022

On February 23, 2022 the European Commission published its long-awaited [proposal](#) for a Corporate Sustainability Due Diligence Directive (“Directive”). The aim of the Directive is to better exploit the single market to prevent and mitigate adverse human rights and environmental impacts in corporate and financial actors’ value chains.

The Directive would require subject “companies” (broadly defined to include corporate and financial actors) to implement a sustainability due diligence strategy to address adverse human rights and environmental impacts (“adverse impacts”) across their global value chains. Adverse impacts include violations of a broad range of environmental and human rights, among others, rights to life, health, adequate housing, and a healthy environment; labour and indigenous peoples’ rights; and modern slavery and human trafficking norms.

It would also require certain subject “companies” to have a plan to ensure that their business strategies are compatible with limiting global warming to 1.5 °C in line with the Paris Agreement.

### Sustainability due diligence strategy requirements

“Companies” subject to the Directive (including US and other international “companies” doing business in the EU) would need to comply with prescriptive requirements to demonstrate that they take a robust approach to managing environmental and human rights risks across their value chains (upstream and downstream activities relating to the production of goods or the provision of services).

The required sustainability due diligence strategy would need to encompass a robust due diligence policy framework and management system to ensure that “companies”:

- take appropriate measures to identify adverse impacts arising from their own operations, subsidiary operations and certain business relationships with contractors, sub-contractors and other legal entities in the value chain. Such measures should reflect, among other things, the corporate and financial actors’ sector and bargaining power;
- prevent, mitigate and minimise adverse impacts through prevention or corrective action plans; contractual frameworks that are cascaded across the value chain (compliance with which is independently verified); investment in management and production processes; targeted support to SMEs to assist them to comply with codes of conduct and action plans; and collaboration with other businesses within the bounds of competition law;
- refrain from entering into new or extending existing contracts and, where legally possible, suspend or, as a last resort, terminate business relationships, where adverse impacts cannot be addressed;
- develop a complaints mechanism accessible to affected stakeholders, trade unions and civil society organisations. Such mechanism would need to provide for follow up to requests for information and meetings between company representatives and complainants;
- undertake periodic assessment and systems monitoring at least every 12 months; and
- include disclosures in annual reports (for EU “companies”) or otherwise on public-facing websites.

“Companies” that meet a €150 million threshold, regardless of where they are based, will need to adopt a plan to ensure that their business model and strategy is compatible with a 1.5°C transition pathway. Where climate change is a principal risk, emissions reductions objectives will need to be included in the plan.

## Who would the Directive apply to?

The Directive applies to “companies,” which is broadly defined to include, but is not limited to: EU-incorporated companies and partnerships; non-EU-incorporated companies and partnerships; banks; investment firms; AIFMs; insurance companies; pension funds; UCITS management companies; AIFs; UCITS; and Central Clearing Parties.

The Directive applies globally and spans all industries.

Company location/type	Turnover threshold	Employee threshold
EU	Net worldwide turnover of more than €150 million in the last financial year for which annual financial statements were prepared	500+
EU (where at least 50% of net worldwide turnover is generated in one or more high-impact sectors, such as minerals, extractives, agriculture, textiles and garments, excluding where financial actors invest in these sectors)	Net worldwide turnover of more than €40 million (but not more than €150 million) in the last financial year for which annual financial statements were prepared	250+
Non-EU	Net turnover of more than €150 million generated in the EU in the financial year preceding the last financial year	None
Non-EU (where at least 50% of net worldwide turnover is generated in one or more high-impact sectors)	Net turnover of more than €40 million in the EU (but not more than €150 million) in the financial year preceding the last financial year	None

## How would the Directive be enforced?

The Directive proposes regulatory supervision at both the national and European levels. At the European level, the Commission would set up a new European Network of Supervisory Authorities to bring together representatives of the national regulators to ensure a coordinated approach to supervision and enforcement. Regulators would

have powers to request information, carry out investigations and inspections, impose civil penalties and fines (based on turnover) and adopt interim measures to avoid serious risks of harm.

Civil liability provisions are also included to make it easier for third-party claimants to pursue litigation against “companies” in European Member States where non-compliance with the requirements results in loss or damage.

## Next steps

The proposal will now go to the European Parliament and the Council for approval. It is difficult to predict the level of debate that the proposal will receive given the differences to the report adopted by the European Parliament in 2021 that contained an initial draft proposal. Once adopted, Member States will have two years to transpose the Directive into national law and communicate the relevant texts to the Commission.

Global companies and financial actors may want to consider which entities within their organisations are in scope of the Directive. If they are in scope, they may need to undertake a gap analysis to understand the gaps between existing policies, procedures and operational nuances and requirements of the Directive.

## Authors

Ruth Knox

Partner / London

Daniel D'Ambrosio

Associate / London

Sara K. Orr

Partner / Chicago

Jennie Morawetz

Partner / Washington, D.C.

# Related Services

## Practices

- Transactional
- ESG & Impact

## Suggested Reading

- 08 November 2022 - 10 November 2022 Sponsored Event PERE America Summit 2022
- 13 June 2022 - 15 June 2022 Sponsored Event Kayo Women's Private Equity and ESG Investment Summits
- 22 May 2022 - 24 May 2022 Sponsored Event IBA Annual Conference on the Globalisation of Investment Funds

This publication is distributed with the understanding that the author, publisher and distributor of this publication and/or any linked publication are not rendering legal, accounting, or other professional advice or opinions on specific facts or matters and, accordingly, assume no liability whatsoever in connection with its use. Pursuant to applicable rules of professional conduct, portions of this publication may constitute Attorney Advertising.

© 2022 Kirkland & Ellis LLP.