



REWARD VALUE

THE PROPOSED DIRECTIVE ON CORPORATE SUSTAINABILITY DUE DILIGENCE: A CRITICAL ANALYSIS

WORKING PAPER

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Executive remuneration today is driven by incentives that may no longer align with shareholder interests or reflect broader societal responsibilities.

Reward Value Foundations' mission is to support the development of remuneration policies that contribute to long-term sustainable and inclusive value creation. The Foundation seeks to further the debate on executive remuneration with investors, business schools, and the business community at large to develop evidence-based, long-term, sustainable, and stakeholder-inclusive executive remuneration policies.

Reward Value Foundation is a not-for-profit research initiative. Reward Value can be reached by email (contact@rewardvalue.org). For more information on Reward Value please visit our website www.rewardvalue.org.

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EXECUTIVE SUMMARY

Reward Value welcomes the European Commission's proposal for a Corporate Sustainability Due Diligence Directive (CSDDD proposal). The need for companies to take accountability for their value chains and sustainability practices is pressing, and the EC's response is both relevant and helpful in developing solutions to these issues. However, as this analysis sets out, several key elements of the proposal are lacking, or problematic in their formulation.

The CSDDD proposal enshrines aspects of established international instruments, for example the United Nations' Guiding Principles on Business and Human Rights (UNGPs), into European Union (EU) legislation. This translation of soft to hard law follows a trend that has been taking place at Member State level for some time. This alignment, specifically between EU law and the UNGPs, is desirable as policy coherence enhances legal predictability, as well as facilitates compliance. However, this process can pose difficulties – namely, as we find here – with departures both from soft law and best practices. New legislation also always poses the double risk of generating perverse incentives, as well as overregulation.

There are several aspects of the CSDDD proposal that indicate that the EC might have lost a degree of confidence originally expressed in the ambitions of the Sustainable Corporate Governance Initiative. This can partially be attributed to the critical reaction to the foundational studies the EC used to formulate its consultation questionnaire, though other pressures from the market are undoubtedly also at play. Where their confidence has remained strong is in the regulation of human rights and environmental due diligence (HREDD) – a concept already enshrined in some of the Member States' legal systems. However, in other sections of the proposal, sustainability has been constrained to a single environmental angle, effectively discouraging broader approaches.

The proposed CSDDD is very limited in its scope of application, and critics have raised the issue of whether the hope of 'spillover', in lieu of hard incentives, has not been too heavily relied on when considering SMEs in larger companies' value chains. This scope is a particular departure from the UNGPs, as well as a possible misalignment with existing EU legislation.

The scope of the CSDDD proposal is further problematic with regards to its calculation of turnover, which is preferential towards non-EU companies. Once again, there is a case for spillover to occur; in keeping with the EU's attempt to limit extraterritorial jurisdiction. However, the way in which an attempted balance is struck here may open the door to strategic rearrangements of company value chains in order to evade liability.

The CSDDD proposal establishes a human rights and environmental due diligence (HREDD) obligation. In line herewith, companies are expected to create a HREDD policy under which (potential) adverse human rights and environmental impacts are identified and prevented or ended. At a glance, this development fosters awareness in board rooms, as well as facilitates disclosure and stakeholder engagement. However, these provisions depart from international standards, and conflict with best practices concerning the categorisation of human rights in international law, particularly regarding the emphasis on 'violations' and the definitions of 'environmental impacts'. Further issues with these provisions include the use of the term 'appropriate measures' when describing a company's actions in identifying and preventing or ending (potential) human rights and environmental adverse impacts. This term creates what can be understood as a 'reasonableness test' to be applied in courts, which may create an unfair burden of proof on those seeking legal remedies. The scope with which companies should analyse their risks in this domain also create several potential issues, namely with the CSDDD proposal's limitation to a company's "established business

relationship [network]”, another provision departing from best practices and creating perverse incentives. The method of implementation offered to companies, namely contractual assurances, is here utilised once again in the hope of “spillover” by encouraging companies to leverage their contractual power to spread HREDD compliance through their supply chain. However, critics mention that this may shift responsibility away from the reporting company and encourage tick-the-box compliance. The proposal also makes reference to stakeholder consultation in the context of HREDD provisions; however, the formulations of these obligations are weak and significantly undermine the goal of meaningful consultation.

The CSDDD proposal establishes a fault-based liability regime to ensure (potential) victims of adverse human rights and environmental harms are compensated. This liability is subject to a reasonableness test, whereunder the actions of a company causing adverse human rights infringements and environmental harms must have been unreasonable in the circumstances in order for liability to ensue. This test seeks to strike a balance between access to remedy for victims, and mitigating litigation risk on companies. However, critics have expressed doubts as to the fairness of these provisions, considering the CSDDD proposal makes no effort to reverse the burden of proof, thereby creating an overly high threshold for potential victims to prove their case.

Under the proposed CSDDD, the director’s duty of care is broad, including the obligation to consider sustainability concerns, human rights, climate change and environmental consequences of the tasks carried out in their position. The ensuing liability imposed upon directors is personal in nature and foresees the payment of damages to the company should the director breach the duty of care. This provision has been compared to section 172 of the UK Companies Act, though its content is both more vaguely construed and subject to higher levels of criticism than its British counterpart.

Executive remuneration is addressed only briefly by the CSDDD proposal, and its provisions are given little potential for driving change: limited to certain situations and in consideration of very specific metrics – notably, environmental. In providing such restricted space to executive remuneration, and in some cases actively discouraging engagement herewith, the drafters of the CSDDD proposal have missed an opportunity to align with and support wider goals of the original initiative.

Long-term value creation and interests are a fundamental component of the concept of sustainability. Following the backlash to the foundational studies to the CSDDD proposal consultation document, the EC distanced itself from the concept of ‘short-termism’ in corporate governance. This resulted in the proposal at hand lacking a strong position on the temporal element of sustainability, and in particular, a guiding definition of ‘long-term’. Another important element missing from the proposal text is that of ‘ESG’ - which has become a popular set of metrics in corporate governance, and the financial sector. This latter sector, in particular, was addressed only briefly in the CSDDD proposal, due to it being viewed as ‘low-risk’ for HREDD and other sustainability concerns. This contrasts starkly with the best practices already in existence at financial institutions.

Sustainability, as a core element of this proposal, is notably treated with only a vague definition. Given the centrality of this issue in policymaking worldwide and particularly in the EU, a refocusing of the notion of sustainability around a single point of reference – humanity and human rights, which would foster policy coherence and clarity, is desperately needed.

INTRODUCTION

Two years have elapsed from the first steps of the European Commission's Sustainable Corporate Governance Initiative.¹ Following an intense period of preparations, research and consultations with experts and interested parties, the long-awaited outcome of the initiative was finally published on the 23rd of February 2022, in the form of the proposal for a Directive on Corporate Sustainability Due Diligence (CSDDD proposal).² The proposed Directive, submitted together with a 26-page long Explanatory Memorandum, has been the subject of scrutiny and commentary from a wide range of stakeholders. After having published a short reaction to the CSDDD proposal in April 2022,³ Reward Value Foundation (Reward Value, the Foundation) now seeks to provide a more comprehensive, in-depth analysis, building on the commentary and discourse that has been flourishing around the proposed Directive, and based on the Foundation's experience in researching sustainable corporate governance and sustainable executive remuneration. Reward Value welcomes the CSDDD proposal as an important next step towards a sustainable and inclusive economy. We recognise the Commission's effort to introduce and prioritise sustainability in European corporate governance and we appreciate the strengthening of the role of human rights and environmental concerns in light of companies' contribution to the sustainable development and sustainable transition of economies. In particular, we welcome the creation of a harmonised framework for human rights and environmental due diligence (HREDD), and we support the Commission's effort to further align with international standards like the UN Guiding Principles on Business and Human Rights (UNGPs, Principles) to increase awareness and accountability in relation to human rights and environmental harm, and to foster the inclusion of stakeholder value in corporate governance. In general, due diligence being integrated into a company's business strategy supports a systematic consideration of human rights, environmental and governance risks to be embedded across all activities of firms and their value chains. Therefore, the CSDDD proposal represents an important step forward for a sustainable evolution of governance practices.

In light of the proposed CSDDD's important achievements in these regards and having closely considered the feedback received by the proposal in the past few months, Reward Value here joins the chorus of commentators in the effort to highlight areas of potential improvement. Currently the proposed Directive has not yet been adopted and is undergoing the co-decision procedure in the European Union. At this time, there is still room for amendments by the European Parliament and Council. As anticipated in the Foundation's shorter response, this article seeks to comment on the sentiment of unfulfilled expectations expressed by several stakeholders and to invite the co-legislators to reconsider certain aspects of the CSDDD proposal, in order to unlock what we believe is its full potential as a transformative and influential instrument for sustainable corporate governance before its adoption. To this effect, we would also like to stress the need for a strong enforcement mechanism to ensure the structural changes the Directive seeks to achieve are fully enshrined. Reward Value Foundation's position on the Directive is grounded in the belief that proactive intervention in the area of sustainable corporate governance is needed, and that executive remuneration can be leveraged to incentivise behavioural changes in corporate governance practices.⁴ Moreover, since sustainability in itself is a long-term concept, Reward Value supports the idea that such time orientation should be better reflected in corporate governance.⁵

¹ See: European Commission, [Sustainable corporate governance](#).

² European Commission (2022) Proposal for a Directive of the European Parliament and of the Council on Corporate Sustainability Due Diligence and amending Directive (EU) 2019/1937, 2022/0051 (COD), COM(2022) 71 final (CSDDD proposal).

³ Reward Value Foundation (2022) Response to the Proposed Directive on Corporate Sustainability Due Diligence.

⁴ Reward Value Foundation (2020) Green Paper - Reward Value.

⁵ Reward Value Foundation (2021) Managerial and Capital Market Short Termism.

Lastly, we seek to highlight the need for companies to be aware and prepare in anticipation to the proposal's implementation.⁶ Once adopted by Council and Parliament, Member States will have two years to transpose it into national law.⁷ At this point, the CSDDD Directive will be binding on companies falling under its scope of application. In this transitory period, companies should consider making the necessary assessments and preparations and ready themselves to comply with the Directive's requirements.⁸ The same advice is also extended to non-European Union (EU) companies, given the extraterritorial application of the proposal.⁹

This article is divided in two main parts: the first part, 'An Assessment', analyses the characteristics and implications of key articles in the CSDDD proposal, starting from the subject matter, the scope of application, the content of the HREDD obligation, the provisions on civil and personal liability and, finally, executive remuneration. In the second part, 'Considerations', the article dives into broader commentary on the CSDDD proposal's approach to sustainability and the nature of the policy-making process that has resulted into the finalised version of the proposed Directive.

PART 1 – AN ASSESSMENT

SUBJECT MATTER

As laid out in Article 1, cited below, the subject matter of the proposed Directive encompasses obligations (and liability) for companies regarding human rights and environmental impacts, with respect to their own operations, the operations of their subsidiaries and the actions of entities along the value chain with which the company has an established business relationship:

Article 1 Subject matter

1. This Directive lays down rules

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

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

The goal of the Directive is to enshrine principles and concepts pertaining to international soft law into EU hard law,¹⁰ as well as extend to the whole European Union some legislative developments pioneered in the past few years by some Member States.¹¹ Regarding the influences from international soft law, the proposed Directive makes explicit reference to key documents which have provided a blueprint for the CSDDD's conceptualisation of HREDD and corporate responsibility for human rights and environmental harms.¹² In this regard, the UN Guiding Principles for Business and Human Rights is one of the most important foundational

⁶ Article One (2022) EU Commission Proposal–Corporate Sustainability Due Diligence Directive, Briefing Note No. 2 p.7.

⁷ More specifically, provisions pertaining to group 1 companies (falling under Article 2(1), point (a), and Article 2(2), point (a)) have to be transposed within 2 years, whereas provisions pertaining to Group 2 companies (referred to in Article 2(1), point (b), and Article 2(2), point (b)) have a deadline of 4 years. See: CSDDD proposal Article 30.

⁸ For an example of available resources regarding doubts and commonly asked questions on the CSDDD proposal and how it will work see: [A Q&A on the European Commission's Proposed Corporate Sustainability Due Diligence Directive](#).

⁹ Knapp (2022) Proposed EU Directive on Corporate Sustainability Due Diligence: Why Non-EU Business Should Respond to the Consultation, Oxford Business Law Blog.

¹⁰ See: United Nations. (2011). Guiding principles on business and human rights: Implementing the United Nations "Protect, Respect and Remedy" framework; OECD (2011), OECD Guidelines for Multinational Enterprises, OECD Publishing.

¹¹ See: Law No. 2017-399 (2017) Duty of Vigilance of Parent and Instructing Companies.

¹² CSDDD proposal, Preamble p. 28.

instruments of the CSDDD.¹³ As the first international authoritative set of soft law standards of businesses, States and stakeholders, the UNGPs have been incredibly influential for norm development in the field of CSR and human rights both at national and international level.¹⁴

From a policy standpoint, it is desirable for European legislation to conform and align with existing instruments like the UNGPs.¹⁵ Departing from such highly authoritative standards, which are already established and widely used in the market, would risk generating uncertainties, and heightened compliance costs for companies, as well as policy confusion. Referring to these instruments also strengthens their legitimacy and provides market participants with a direct link to an established, structured and practical soft law framework which can aid them in compliance.¹⁶

As the UNGPs have become increasingly used and recognised by international businesses,¹⁷ the Directive's reference and adherence to them is desirable. However, for the reasons mentioned above, the CSDDD proposal has also been closely scrutinised and criticised in key areas in which there seem to be problematic departures from this instrument.¹⁸ As will be addressed in greater depth in the following sections of this article, departing from the UNGPs in some instances could mean departing from established best practices, and more generally it could result in contradicting the fundamental purpose and essence upon which the Principles were created.¹⁹

In this regard, the proposal shines a light on the difficulties of the hardening of soft law instruments and opens up the question of whether - and to what extent - it is more effective to regulate through hard law provisions or to rely on more flexible, voluntary tools. The decision-making process towards the drafting of the Directive represents a balancing act between these two different types of tools and reflects a trend towards the integration of soft law into hard law.²⁰ Whether the increasing reliance on hard obligations will lead to structural changes in corporate governance or conversely enable a tick-the-box mentality in market participants, remains to be seen. This will also very much depend on the quality of the policy. In light of the increasingly complex interactions between hard and soft law-based policy tools, there definitely is a need for updated empirical research on the effectiveness of hard vs soft law. On this very same note, a key aspect to keep in mind when considering the policy-implications of the CSDDD proposal is the danger of overregulation, especially in relation to other EU policies and the lack of coherence between such laws. Overregulation is a concept that is frequently brought up in the discourse around the regulation of corporate governance and that will recur in following sections of this article. When regulating matters like the ability of directors to make business decisions, or the autonomy of companies to organise their internal structure and business operations, the dangers posed from a rigid top-down approach are many. Hard law regulation in this regard can easily be inefficient as well as ineffective and the right balance should be struck with regard to ensuring that market participants stay within certain boundaries, while maintaining their ability to innovate and pursue tailored solutions.

¹³ CSDDD proposal, Preamble, para (5) p. 28 and (12) p. 30.

¹⁴ CSDDD proposal, Explanatory Memorandum p. 11.

¹⁵ Holly & Andreasen Lysgaard (2022) Legislating for impact: analysis of the proposes EU Corporate Sustainability Due Diligence Directive p.4; Shift (2022) The EU Commission's Proposal for a Corporate Sustainability Due Diligence Directive - Shift's Analysis p. 3.

¹⁶ CSDDD proposal, Preamble, para (26) p. 35.

¹⁷ Holly & Andreasen Lysgaard (2022) Legislating for impact: analysis of the proposes EU Corporate Sustainability Due Diligence Directive p.7.

¹⁸ E.g. O'Brien (2022) Sustainable corporate governance: submission to Consultation on European Commission's proposal for a Directive on corporate sustainability due diligence COM(2022)71 final. Holly & Andreasen Lysgaard (2022) Legislating for impact: analysis of the proposes EU Corporate Sustainability Due Diligence Directive; Lafarre (2022) Mandatory Corporate Sustainability Due Diligence in Europe: The Way Forward, the ECGI Blog; Shift (2022) The EU Commission's Proposal for a Corporate Sustainability Due Diligence Directive - Shift's Analysis.

¹⁹ Lafarre (2022) Mandatory Corporate Sustainability Due Diligence in Europe: The Way Forward, the ECGI Blog.

²⁰ See the French Duty of Vigilance Law of 2016; Law No. 2017-399 (2017) *Loi de Vigilance*.

As mentioned above, the CSDDD proposal also serves to take some key legislative developments that have occurred at Member State-level in the past few years and harmonise them at EU level.²¹ This is particularly true for the parts of the Directive establishing HREDD obligations. In this regard, a particularly influential piece of legislation is the French *Loi de Vigilance* of 2016,²² also clearly inspired by the UNGPs, which established supply-chain HREDD obligations for French companies of a certain size. The success and popularity of the Vigilance Law, coupled with the fact that other Member States have started to follow the French example in this area,²³ are likely factors that have led the Commission to seek Union-level harmonisation on this topic.²⁴ On the same note, similarities have been drawn between the proposal's articles on directors' duty of care and the section 172 of the UK's Companies Act, often referred to as the cornerstone of the UK's 'enlightened shareholder model'. When considering that certain States have already started legislating on these topics independently, it should be also kept in mind that, being a Directive, the CSDDD proposal will have to be transposed into national law by each EU Member State. Assuming the proposal will function as a minimum harmonisation Directive, this means that States will be free to set higher standards and thresholds than those provided in the proposed text and, consequently, there may be varying degrees of differences in the national implementations of the provisions.²⁵

The influences and implications of the CSDDD proposal's relationship with soft law and national law developments will be addressed throughout this document. Having established the broader framework in which the proposal was conceptualised, the following passages seek to analyse in greater depth key parts of the Directive, their characteristics, and their legal implications.

SCOPE OF APPLICATION

The scope of application of the CSDDD proposal is also often referred to as the 'personal scope'.²⁶ Thus, the personal scope indicates to which companies the Directive applies – i.e. which companies will have to follow the provisions set out in the text. Conversely, the substantive content of those provisions is referred to as the 'material scope' – i.e. what exactly is included in the due diligence obligation. The specifics of material scope will be addressed in more detail further on.

The personal scope of the Directive is established by Article 2, which stipulates that the proposal shall apply to large EU and non-EU companies, as well as medium EU and non-EU companies in 'high impact sectors'.²⁷ 'Large' and 'medium' enterprises are so determined in accordance with their turnover, as well as their geographical area of operation. For EU-based companies, the CSDDD proposal considers global turnover, whereas for non-EU companies, only turnover generated in the EU is relevant.²⁸ In the Explanatory Memorandum,²⁹ the group of 'large' companies subject to the scope of the proposal (both EU and non-EU-based) is referred

Group 1 Companies

- 500+ employees;
EUR 150M turnover.

Group 2 Companies

- 250+ employees;
EUR 40M turnover.

²¹ According to commentators the EU-level harmonization of HREDD regulation is reportedly one of the reasons the proposed CSDDD has attracted business support, as it enhances legal cohesion and predictability: The Raoul Wallenberg Institute (2022) *The EU Directive on Corporate Sustainability Due Diligence: origins, compliance effects and global significance*.

²² Law No. 2017-399 (2017) *Loi de Vigilance* (Duty of Vigilance of Parent and Instructing Companies).

²³ See for example: *Lieferkettensorgfaltspflichtengesetz* (Act on Corporate Due Diligence Obligations in Supply Chains), BGBl I 2021, 2959.

²⁴ For an overview of the entrenchment of soft law into European legal systems, with a particular focus on French law and its relationship to the CSDDD proposal, see: Pietrancosta (2022) *Codification in company law of general CSR requirements: pioneering recent French reforms and EU perspectives*, ECGI.

²⁵ Article One (2022) *EU Commission Proposal—Corporate Sustainability Due Diligence Directive*, Briefing Note No. 2 p7.

²⁶ CSDDD proposal, Explanatory Memorandum p. 15.

²⁷ See: CSDDD Article 2.

²⁸ CSDDD proposal Article 2 (1) and 2(2).

²⁹ CSDDD proposal, Explanatory Memorandum p. 1- 26.

to as 'group 1',³⁰ whereas the group of 'midcap companies in high-risk sectors' (both EU and non-EU-based) is referred to as 'group 2'.³¹ The CSDDD proposal, in certain cases, imposes different obligations on the two different groups.³²

As remarked in the proposal itself, small and medium enterprises (SMEs) are excluded from the application of the Directive and that, indeed, only 1% of companies operating in the Union are to be subject to the due diligence obligation introduced by the proposal.³³ As it is, the formulation of Article 2 has been analysed and criticised since the publication of the proposal.³⁴ The following subsections elaborate on some relevant points of discussion relating to Article 2 in particular and the implications of the applicability of the CSDDD proposal in general.

Personal Scope
What companies fall under the scope of the CSDDD?

Scope and effectiveness: too limited?

First and foremost, the CSDDD proposal has been criticised for its limited scope of application which, as many have pointed out, could greatly hinder its effectiveness.³⁵ To understand the choices made regarding the formulation of Article 2, certain considerations should be kept in mind: first of all, the formulation addresses the concern of an excessive burden and heightened compliance costs on SMEs. This approach allows the big enterprises that have the appropriate resources to take the lead and establish best practices on HREDD in the EU market, thereby setting an example which could be followed by SMEs in due time. In addition, it can be assumed that this '1% of large companies' is connected to a great number of SMEs through an intricate net of contractual relationships, and complex value chains. Given this fact, it is foreseeable that imposing the proposal's obligation on even a small number of parent companies should generate a significant spillover effect in the EU market. This is consistent with the general approach of the EU when legislating on corporate matters,³⁶ which often emphasises the need for SMEs to be supported and encouraged towards compliance over time. Having said this, as pointed out by critics of the proposal, it is debatable whether sufficient incentives have been established for this purpose.³⁷

Another common criticism regarding the formulation of Article 2, regards the choice of 'high impact sectors'. As mentioned before, 'group 2' companies are enterprises that do not meet the turnover thresholds of group 1 but are nonetheless subject to certain parts of the CSDDD proposal given the 'high risk nature' of their business operations.³⁸ The criticism stems from the fact that the list of 'high-impact sectors' identified in CSDDD proposal Article 2 (1)(b) seems to be unduly limited, thereby excluding other equally high-risk sectors.³⁹ For example, construction, infrastructures, energy, transport, logistics, electronic, auditing and the

³⁰ CSDDD proposal Articles 2(1)(a) and 2(2)(a).

³¹ CSDDD proposal Articles 2(1)(b) and 2(2)(b).

³² E.g. CSDDD proposal Article 15 only applies to 'group 1' companies.

³³ CSDDD proposal, Explanatory Memorandum p. 15.

³⁴ E.g. Business & Human Rights Resource Centre (2022) [UN Working Group on Business and Human Rights preliminary assessment of EU draft due diligence directive](#); PRI (2022) [PRI statement: European Commission proposal on Corporate Sustainability Due Diligence](#); Human Rights Watch (2022) [EU: Disappointing Draft on Corporate Due Diligence](#); ShareAction (2022) [EU presents watered-down rules on Corporate Sustainability Due Diligence](#); Investor Alliance for Human Rights (2022) [Investor Alliance for Human Rights Responds to EU Directive on Corporate Sustainability Due Diligence](#) etc.

³⁵ Id *ibid*.

³⁶ See for example: the Sustainable Finance Disclosures Regulation (Regulation (EU) 2019/2088, SFDR) ; the Non-Financial Reporting Directive (Directive 2014/95/EU, NFRD); etc.

³⁷ Id. *ibid*.

³⁸ CSDDD proposal Articles 2(1)(b) and 2(2)(b).

"The definition of high-impact sectors has been limited to sectors with high risk of adverse impacts and for which OECD guidance exists" CSDDD proposal, Explanatory Memorandum p. 21.

³⁹ O'Brien (2022) Sustainable corporate governance: submission to Consultation on European Commission's proposal for a Directive on corporate sustainability due diligence COM(2022)71 final p.7; Holly & Andreassen Lysgaard (2022) Legislating for impact: analysis of the proposed EU Corporate Sustainability Due Diligence Directive p. 10.

financial sectors are excluded. Additionally, other factors such as the stability of the territories in which business operations are carried out, are not considered, which reflects a limited understanding of ‘high impact’ and ‘high risk’. It should be also pointed out that the size and annual turnover rate are not necessarily reliable indicators of a company’s impacts and influences over its value chain. Ultimately, the personal scope of the Directive as formulated leaves out many harmful business operations.⁴⁰

It has been noted that the restricted approach to the scope of application of the proposal, as well as the uncertainties related to the feasibility of a ‘spillover effect’ to spread compliance amongst SMEs, might conflict with the purpose of the international soft law instruments which are foundational to the CSDDD proposal. Notably, the UNGPs establish the responsibility of “*all enterprises*” to respect human rights, “*regardless of size*” (although the different scale of means and resources available to companies of different dimension is acknowledged).⁴¹ With its narrower scope, the proposal fails to acknowledge that all companies can harm human rights and the environment, regardless of size.

Other than failing to align with the UNGPs, some have pointed out that the restricted personal scope of the Directive may even be a departure from emerging practice.⁴² Ideally, the CSDDD proposal should provide for specific measures in support of SMEs and micro-enterprises as well as a degree of proportionality built into the due diligence process relating to the degree of risk a company is exposed to. Such an approach would circumvent the need for a spillover effect with all its uncertainties and follow more closely the blueprint of the UNGPs. Ultimately, departing from the Principles and best practices may have a chilling effect and perversely incentivise companies and market actors to go back on their progress and opt for a literal and minimalistic interpretation of the new law, once in effect (see the abovementioned points on the dangers of overregulation).⁴³ This outcome is to be avoided, as any HREDD process must cover the entire value chain of an undertaking.

Other issues related to these inconsistencies will be elaborated upon in later parts of this article as well, particularly with regard to the material scope of the Directive. However, it should be noted here that inconsistencies can also be found between the CSDDD proposal and other EU law. Most notably, as the proposal does not impose disclosure obligations, the Explanatory Memorandum refers to the Commission’s recent proposal for a Corporate Sustainability Reporting Directive (CSRD),⁴⁴ which should complement the CSDDD proposal in this regard.⁴⁵ It is notable, however, that the two proposals have a similar, but slightly different size thresholds,⁴⁶ meaning that not all companies affected by the proposed CSDDD would be required to report on their sustainability under the CSRD.⁴⁷

The CSDDD proposal and the CSRD are intended to be “mutually reinforcing”.⁴⁸ Given this complementarity, several questions arise to the misalignment of personal scope under the respective Directives. Taking an EU-

⁴⁰ European Parliament (2022) Corporate sustainability due diligence: Could value chains integrate human rights and environmental concerns? p. 8.

⁴¹ See: UNGPs Principle 14.

⁴² Holly & Andreasen Lysgaard (2022) Legislating for impact: analysis of the proposed EU Corporate Sustainability Due Diligence Directive p. 10; Shift (2022) The EU Commission’s Proposal for a Corporate Sustainability Due Diligence Directive – Shift’s Analysis p.5.

⁴³ See on the chilling effect of SRD II on Stewardship Codes: Dionysia Katelouzou, Konstantinos Sergakis (2020) When Harmonization is Not Enough: Shareholder Stewardship in the European Union.

⁴⁴ European Commission, ‘Proposal for a Directive of the European Parliament and of the Council Amending Directive 2013/34/EU, Directive 2004/109/EC, Directive 2006/43/EC and Regulation (EU) No 537/2014, as Regards Corporate Sustainability Reporting’, *Official Journal of the European Union* O104, no. 537 (2021): 1–65 (CSRD).

⁴⁵ CSDDD proposal, Explanatory Memorandum p. 4

⁴⁶ The CSRD applies to “1. All large companies with 250 employees or more, regardless of a capital market orientation. The second threshold for large companies continues to be a turnover of > 20 million euros or sales of > 40 million euros.

2. All capital market-oriented small and medium-sized enterprises, except for micro-enterprises (from 01.01.2026). According to Directive 2013/34/EU, companies are considered small if they exceed two of the three characteristics 1) 10 employees, 2) 350,000 euros total assets and 3) 700,000 euros net sales”.

⁴⁷ See: Travers&Smiths (2022) [Corporate Sustainability Due Diligence: A long-awaited proposal revealed.](#)

⁴⁸ Bolognesi (2022) Briefing: EU Corporate Sustainability Due Diligence Legislative Proposal. In *Amfori*. p 7.

based company as an example, compliance with the CSRD would be necessary where the company is listed, or where at least two of the three following criteria are fulfilled:

- 250 employees;
- €40 million annual turnover;
- €20 million total assets;⁴⁹

Several exceptions exist with relation to SMEs. Notably, micro-enterprises are also excluded from the scope of application, irrespective of whether they are a listed entity or not.⁵⁰ Conversely, this same EU-based enterprise would only be required to seek compliance with the proposed CSDDD where their number of employees exceeds 500 and where their total turnover exceeds 150 million.⁵¹ This apparent mismatch of scope has been the subject of commentary from many sources, including national governments, who will, as mentioned, be tasked with transposing the Directive into national law.

A rudimentary analysis of the interaction between these two scopes indicates that this mismatch is without consequence – in that a company who falls under the scope of the CSDDD proposal would automatically fulfil the criteria of the CSRD’s application, but not vice versa. However, some commentary suggests that some companies may be able to exploit a gap, though details of this apparent lacuna have not been forthcoming.⁵² Aside from amending the Proposal itself, a solution to this situation may lie in the upwards harmonisation of the Directive at the time of national transposition by member states. The Dutch government, for example, intends to lower the threshold for applicability of the CSDDD proposal, thereby aligning with those criteria set out by the CSRD.⁵³ For a more detailed discussion of the CSRD, see our forthcoming background note.

Another important piece of legislation which intersects with the CSDDD is that of the Alternative Investment Fund Managers Directive (“AIFMD”).⁵⁴ This Directive, effective since 2013 and which is currently under revision by the Commission, provides a framework for regulation of alternative investment instruments such as hedge funds, private equity funds and real estate investment funds.⁵⁵

The financial sector has seen a large number of proposals for sustainability-related disclosure legislation over the past two years – the EU Taxonomy,⁵⁶ the CSRD, and the SFDR.⁵⁷ In order for the various disclosure obligations and mechanisms under the proposed laws to have their desired effect in rendering the financial services sector more transparent about their contributions towards a sustainable economy, care must be taken for coherence and balance. Indeed, the introduction of the CSDDD proposal poses several questions with regards to the alternative investment fund managers (“AIFMs”). Notably, the proposed CSDDD lacks clarity on its scope of application with regards to the services provided by AIFMs, the due diligence obligations as they apply to certain types of undertakings, as well as the implication of the term ‘high-impact sector’ regarding investments and the understanding of a ‘value chain’ in financial services.⁵⁸

⁴⁹ CSRD Recital 14.

⁵⁰ European Commission (2022) Corporate Sustainability Reporting.

⁵¹ CSDDD proposal Article 2.

⁵² von den Bogart (2022) 10 Things to Know About the EU Corporate Sustainability Due Diligence Proposal.

⁵³ Dutch Banking Association (2022) Consultation Feedback: Key Messages - EC Directive on Corporate Sustainability Due Diligence. (CSDDD) Stibbe (2022) Proposal for a Directive on Corporate Sustainability Due Diligence. In Stibbeblog.

⁵⁴ Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010 (AIFMD).

⁵⁵ AIFMD Recital 4; Article 4.

⁵⁶ Regulation (EU) 2020/852 of the European Parliament and of the Council of 18 June 2020 and on the establishment of a framework to facilitate sustainable investment, investment and amending Regulation (EU) 2019/2088.

⁵⁷ Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on sustainability-related disclosures in the financial services sector.

⁵⁸ Invest Europe (2022) Position paper on the European Commission’s Proposal for a Directive on Corporate Sustainability Due Diligence and amending Directive (EU) 2019/1937. pp2-3.

This being said, there has been relatively little response from the alternative investment community on the implications of the proposed CSDDD on AIFMs, suggesting that the proposal may not disrupt much of the current programming in disclosures made by these entities. Regardless, the disconnect between the CSDDD proposal and the financial sector in general has been noted by various commentators, especially regarding the proposed Directive ability to contribute to the coherence and synergy of the policy frameworks for sustainable governance and sustainable finance in the EU. This point will be addressed in greater depth in the later part of this article.

In light of this overall context, the following paragraphs will explore in greater depth some of the key implications and consequences related to the applicability of the proposal.

Level playing field and the extraterritorial implications

As mentioned above, the CSDDD foresees different approaches as to what type of turnover to consider, when it comes to the applicability of the Directive. For EU-companies, this means global turnover, whereas for non-EU companies only turnover generated in the Union.⁵⁹ This approach seems to be an attempt of establishing a level playing field within the EU market. Considering that, so far, only a few individual EU Member States have enacted national due diligence legislation, the EU initiative definitely widens the level-playing field and improves competition within the internal market. However, commentators have expressed uncertainties regarding the effectiveness of this strategy:⁶⁰ first of all, this application seems to be more favourable to non-EU corporations, as most companies that will be affected will be EU-based.⁶¹ One of the explicit aims of the formulation of Article 2 is indeed to “ensure that third countries are not more likely to fall within the scope”.⁶² Since the CSDDD proposal is a regional piece of legislation, it is expected that the personal scope of the proposed Directive mostly encompass EU companies, addressing competition within the EU. However, given today’s highly globalised economy, international (extra-EU) competition also plays a major factor in the business activities of EU companies, and, in light of this fact, it could be argued that the current text of the proposed Directive leaves such a potential disadvantage for companies insufficiently addressed.

A stated goal of the Directive is to generate a spillover effect and propagate HREDD practices outside the EU.⁶³ However, most non-EU companies that operate in the EU do so through EU-based subsidiaries, meaning that, unless these subsidiaries generate substantial turnover in the EU market alone, they are less likely to fall under the scope of application. Given this fact, non-EU parents would be able to escape liability by operating in the EU through smaller subsidiaries.⁶⁴ Overall, it is fair to state that there are serious doubts in respect to the effectiveness of the desired level playing field and the wording of the current proposed Directive.

The practical implications of the extraterritorial reach of the proposed CSDDD, as well as the feasibility of the ‘spillover effect’ will have to be assessed after the implementation of the Directive.⁶⁵ Should the

⁵⁹ CSDDD proposal Articles 2 (1) and 2(2).

⁶⁰ See: ECGI (2022) Online Policy Workshop – European Commission Directive on Corporate Sustainability Due Diligence.

⁶¹ “While the Directive will cover about 13 000 EU companies, based on the estimations of the Commission, it will only cover about 4 000 third-country companies” CSDDD proposal, Explanatory Memorandum p. 16.

⁶² CSDDD proposal, Explanatory Memorandum p.15.

⁶³ “large third-country companies having a high turnover in the Union have the capacity to implement due diligence and will benefit from the advantages coming with due diligence also in their operations elsewhere” CSDDD proposal, Explanatory Memorandum p. 16.

⁶⁴ Paccès (2022) Supply Chain Liability in the Corporate Sustainability Due Diligence Directive Proposal, the ECGI Blog.

⁶⁵ For an observation of the of the extraterritorial influence of the European Union in general, see: Bradford (2020) The Brussels Effect: How the European Union Rules the World, Oxford Scholarship Online.

extraterritorial reach be considerable, another point to pay attention to in this regard could be the reaction of non-EU home States, which may decide to respond by strengthening the reach of their own legislation with extraterritorial applicability.⁶⁶ The pros and cons of this outcome should be further explored in order to assess the practical consequences it may produce.

Company Groups

Given the current formulation of Article 2, the CSDDD proposal applies to Value Chains but not to company groups. This approach has interesting implications: firstly, in terms of personal scope, non-EU parent companies operating in the Union through a subsidiary would not be subject to the HREDD obligations nor any liability.⁶⁷ Similarly, should a non-EU parent company have both EU-based subsidiaries, and non-EU based subsidiaries, only the former would be subject to the personal scope of the proposed Directive. This configuration means that, within a company group in which different subsidiaries work with the same high-risk countries or high-risk contractors, only the EU-based subsidiaries would have to establish a due diligence framework. The EU-based subsidiary would have no obligations to ensure that the other companies in its group pay attention to human rights or environmental impacts, even when working with the very same high-risk supplier.⁶⁸ Essentially, the proposal's obligations and liability only apply to the EU subsidiary and the latter's due diligence regarding its established business relationships and do not spread to the other branches of the larger company group.⁶⁹ This 'company-by-company' approach significantly reduces the extra-territorial reach of the HRDD obligation and gives parent companies ample opportunity to avoid liability through strategic composition of their group.⁷⁰ Commentators have pointed out how Article 2 may create loopholes and exacerbate the risk of so-called 'supply-chain's strategic disaggregation' (i.e. rearranging supply chain partners to evade liability).⁷¹

These issues caused by the company-by-company approach also seem to frustrate the original purpose and nature of the UNGPs, which strongly emphasise the need for companies to leverage their influence and business relationships to spread human rights due diligence compliance as much as possible.⁷²

Having addressed Article 2 and the personal scope of the proposed Directive, the next main section of this article will focus on the material scope of the CSDDD proposal, HREDD and other implications related to the applicability of the due diligence obligations. In particular, the next section will take a deeper look into the 'established business relationship', 'appropriate measures' and 'contractual assurances' issues, which have become major topics of commentary on the proposal.

⁶⁶ See: ECGI (2022) Online Policy Workshop - European Commission Directive on Corporate Sustainability Due Diligence, 1st Speaker, Paul Davis (on the US Alien Tort Status).

⁶⁷ Paccès (2022) Supply Chain Liability in the Corporate Sustainability Due Diligence Directive Proposal, the ECGI Blog.

⁶⁸ ECGI (2022) Online Policy Workshop - European Commission Directive on Corporate Sustainability Due Diligence, 1st Speaker, Paul Davis.

⁶⁹ It is also unclear whether - under certain circumstances - two companies in the same company group could qualify as having an 'established business relationship', thereby creating the possibility to circumvent the strictly company-by-company application of the material scope. This possibility, however, has not been widely discussed in the discourse surrounding the CSDDD's scope of application.

⁷⁰ "To avoid regulatory arbitrage, Hansmann and Kraakman advocated a simpler rule unlimited shareholder liability towards tort victims with extraterritorial reach." *Id.* *Ibid.*

⁷¹ *Id.* *Ibid.*

⁷² See: UNGPs Principle 19 and commentary p.20-22.

HUMAN RIGHTS AND ENVIRONMENTAL DUE DILIGENCE AND THE MATERIAL SCOPE

Material Scope
What is included in the due diligence obligation?

The 'material scope' of the directive refers to the actual obligations imposed on the companies which fall under the 'personal scope' of the CSDDD proposal. As laid out in the Explanatory Memorandum, the material scope addresses the due diligence obligations and provides specifications as to the particular human rights and environmental impacts that are to be considered to this effect.⁷³ In this regard, the Memorandum also draws attention to the close link between the due diligence obligations and the provisions on directors' duties and liability.⁷⁴ In order to comprehensively address the material scope and its implications, this section will address the areas covered by Articles 4 through 8 of the CSDDD proposal. Respectively, these articles refer to: 'due diligence';⁷⁵ 'integrating due diligence into companies' policies;⁷⁶ 'identifying actual and potential adverse impacts';⁷⁷ 'preventing potential adverse impacts';⁷⁸ and 'bringing actual adverse impacts to an end'.⁷⁹ When needed, reference will also be made to the definitions laid out in CSDDD proposal Article 3 and the Annex. The topics of civil liability and directors' duties of care will be addressed separately in the next main section.

The proposed Directive's due diligence obligation is established in Article 4 and laid out in Articles 5 through 11. Article 5 prescribes that a company's due diligence policy should describe the corporate's approach to HREDD, the processes put in place to achieve its goals to this effect and a code of conduct to be implemented throughout the value chain. For this purpose, a HREDD policy consists of an ex-ante analysis of the company's operation, as well as the operations of its subsidiaries and contractors,⁸⁰ and what is the relation of these operation to possible human rights and environmental adverse impact. A 'due diligence framework' in this sense should put in place steps and control mechanism aimed at identifying these adverse impacts (CSDDD proposal Article 6), prevent potential adverse impacts (CSDDD proposal Article 7) and bring occurring adverse impacts to an end (CSDDD proposal Article 8). It should be stressed that, by definition, due diligence is an obligation of means, not an obligation of results. While companies are required to put certain procedures in place to address and prevent harms, as long as they adequately implement all necessary measures and procedures, they will not be liable for harm that may still occur.⁸¹ Because of its characteristics, soft law-based (mandatory) HREDD can be a very effective tool to create awareness – especially for the directors – of how the company's business activities relate to –and potentially impact – human rights and the environment. At the same time, the existence of a due diligence framework and policy can facilitate disclosure and allow shareholders and stakeholders to assess a company's approach to sustainability. Notably, in Articles 6, 7 and 8 the proposal encourages companies to consult with stakeholders. Having provided a broad understanding of HREDD as established by the proposed Directive, the next subsections address some key points that have been raised with regard to the CSDDD proposal's material scope, starting with its departure from international standards.

⁷³ CSDDD proposal, Explanatory Memorandum p. 16.

⁷⁴ CSDDD proposal, Explanatory Memorandum p. 16.

⁷⁵ CSDDD proposal Article 4.

⁷⁶ CSDDD proposal Article 5.

⁷⁷ CSDDD proposal Article 6.

⁷⁸ CSDDD proposal Article 7.

⁷⁹ CSDDD proposal Article 8.

⁸⁰ See below the subsection on 'established business relationships'.

⁸¹ "This Directive should not require companies to guarantee, in all circumstances, that adverse impacts will never occur or that they will be stopped. [...] the main obligations in this Directive should be 'obligations of means'. The company should take the appropriate measures which can reasonably be expected to result in prevention or minimisation of the adverse impact under the circumstances of the specific case. [...]" CSDDD proposal, Preamble p. 31-32.

Departures from International Standards

As mentioned, the material scope encompasses the human rights and environmental impacts which would be relevant to a company's HREDD obligations.⁸² The definitions of 'adverse human rights impacts' and 'adverse environmental impacts' are given in Article 3(b) and (c) and, in both instances, the article refers to specific lists that can be found in the proposed Directive's Annex.⁸³

A first point worth mentioning, is that the presentation of human rights impacts in the Annex has been flagged as odd by commentators, as it does not align with the conventional ways of cataloguing human rights.⁸⁴ In addition, rights that have been established in international human rights law for quite some time, have been formulated in novel ways in the CSDDD proposal.⁸⁵ This inconsistent approach creates ambiguities and risks promoting a selective application of standards, which directly conflicts with the principles of indivisibility and interdependence of human rights.⁸⁶ Given these considerations, a more comprehensive, non-limitative, list of human rights instruments would be a more appropriate option.⁸⁷

This departure from established international law is aggravated by the fact that Article 3 defines 'adverse human rights impact' as 'an adverse impact on protected persons resulting from the violation of one of the rights or prohibitions' in the annexes.⁸⁸ As noted by commentators, instruments like the UNGPs and the OECD guidelines very specifically do not use the term 'violation'.⁸⁹ Instead, adverse human rights impacts are usually framed as actions or omissions that infringe on an individual's ability to enjoy their human rights.⁹⁰ Essentially, by requiring the actual or potential existence of a 'violation', the proposal risks limiting the notion of 'impact'. This issue has been criticised as such a formulation and emphasis on human rights violations could unduly raise the threshold for the establishment of corporate responsibility and liability, and thereby reduce the effectiveness of the Directive. Specifically, this aspect ties into the considerations on access to remedy and the burden of proof for victims of human rights adverse impacts.

The UNGPs' approach distinguishes between 'causing', 'contributing to' and 'being directly linked to' risks and adverse human rights impacts.⁹¹ This provides a model for attributing varying degrees of responsibility to companies depending on the specific situation. Adopting this model could better serve the goals of the CSDDD proposal in this regard, and foster policy coherence with the Principles.

In addition to the issues with the categorization of human rights, the CSDDD proposal also presents some shortcomings with respect to the definition of 'environmental impacts'.⁹² In this regard, the Directive makes reference to a limited list of environmental conventions which do not fully address adverse impacts.⁹³ The

⁸² CSDDD proposal Article 6 (1).

⁸³ CSDDD proposal Article 3 (b) 'adverse environmental impact' means an adverse impact on the environment resulting from the violation of one of the prohibitions and obligations pursuant to the international environmental conventions listed in the Annex, Part II; (c) 'adverse human rights impact' means an adverse impact on protected persons resulting from the violation of one of the rights or prohibitions listed in the Annex, Part I Section 1, as enshrined in the international conventions listed in the Annex, Part I Section 2.

⁸⁴ O'Brien (2022) Sustainable corporate governance: submission to Consultation on European Commission's proposal for a Directive on corporate sustainability due diligence COM(2022)71 final p.5; Holly & Andreasen Lysgaard (2022) Legislating for impact: analysis of the proposed EU Corporate Sustainability Due Diligence Directive p. 11-12.

⁸⁵ Holly & Andreasen Lysgaard (2022) Legislating for impact: analysis of the proposed EU Corporate Sustainability Due Diligence Directive p. 13;

⁸⁶ O'Brien (2022) Sustainable corporate governance: submission to Consultation on European Commission's proposal for a Directive on corporate sustainability due diligence COM(2022)71 final p.5.

⁸⁷ European Parliament (2022) Corporate sustainability due diligence: Could value chains integrate human rights and environmental concerns? p. 4. European Coalition for Corporate Justice (2022) *European Commission's proposal for a directive on Corporate Sustainability Due Diligence A comprehensive analysis*, Legal Brief p. 4.

⁸⁸ CSDDD proposal Article 3(b).

⁸⁹ Holly & Andreasen Lysgaard (2022) Legislating for impact: analysis of the proposed EU Corporate Sustainability Due Diligence Directive p. 13.

⁹⁰ Id. *Ibid.*

⁹¹ See: UNGPs Principles 13 and 14.

⁹² On the CSDDD proposal's ability to regulate environmental impacts and challenges thereof, see also: Lindsay (2022) European Commission proposes Mandatory Human Rights and Environmental Due Diligence, *Clifford Chance* p 18-19.

⁹³ See: CSDDD proposal Annex, Part II.

list provided for in the Annex is incomplete and lacks reference to key accords including the Paris Agreement.⁹⁴ Ultimately, these provisions leave a regulatory void which would be better filled by a more general reference to ‘environmental degradation without going into specific lists or conventions.’⁹⁵

Appropriate Measures

When describing how to approach the HREDD policy, CSDDD proposal Articles 6, 7 and 8 indicate that companies should take ‘appropriate measures’ in order to ‘identify, prevent and bring to an end’ potential human rights and environmental adverse impacts. The definition of “appropriate measures” includes “taking into account the circumstances of the specific case, including characteristics of the economic sector and of the specific business relationship and the company’s influence and the need to ensure prioritisation of action”.⁹⁶

Open terms like ‘appropriate measures’ are welcomed in this type of legislation, as they allow for companies to seek out context-specific solutions rather than directing them towards box-ticking exercises. In litigation settings, it also allows for ‘what is appropriate’ to be determined on a case-by-case basis. This is coherent with the fact that the HREDD obligation of the CSDD proposal is an obligation of means. However, this choice of words has been heavily criticised by commentators because of its relation to of the burden of proof. This formulation creates a fundamental test of ‘reasonableness’ (appropriateness) to assess whether the due diligence obligation applies or not in case of alleged violations. Commentators have pointed out how this test will likely prove very difficult to administer in practice.⁹⁷ Most importantly, as explored in a subsequent section on ‘civil liability’, the proposal leaves the question of the burden of proof to the national law of Member States which, as flagged by commentators, overwhelmingly put the evidentiary burden on claimants.⁹⁸ In this case, this means that it is the victims that will have the burden to prove whether the company’s due diligence measures were ‘appropriate’ or not.⁹⁹ By refraining from legislating the burden of proof, the proposed Directive fails to address the issues related to the asymmetry of knowledge and power between large corporations and possible victims, issues which are commonly found in civil liability cases.¹⁰⁰ This is particularly aggravated by the fact that, in order to prove the ‘appropriateness’ of a company’s HREDD measures and to determine whether or not a due diligence duty was breached, potential victims would require access to internal corporate information and, as of now, most EU Member States’ legal systems do not include adequate enough obligations to disclose corporate documents in legal disputes.

In addition to the issue of the burden of proof, it should be pointed out that taking a different approach, such as emphasising the company’s actual and potential ability to influence third parties, as in assessing ‘actual leverage’ and ‘potential leverage’ of the company, would better align with existing international standards. This approach would also give room to encourage companies to increase their leverage when they lack it.

⁹⁴ Other conventions notably missing are: the Ramsar Convention on Wetlands of International Importance Especially as Waterfowl Habitat, the International Convention for the Prevention of Pollution from Ships, the UN Convention on the Law of the Sea, the UN Convention to Combat Desertification or the UNECE Convention on Access to Information, Public Participation in Decision making and Access to Justice in Environmental Matters (Aarhus Convention).

⁹⁵Fore example, this is the approach taken by the French Duty of Vigilance Law. See: Law No. 2017-399 (2017) *Loi de Vigilance*.

⁹⁶ CSDDD proposal, Explanatory Memorandum p. 14.

⁹⁷ ECGI (2022) Online Policy Workshop - European Commission Directive on Corporate Sustainability Due Diligence, 2nd Speaker, Guido Ferrarini.

⁹⁸ European Parliament (2022) Corporate sustainability due diligence: Could value chains integrate human rights and environmental concerns? p. 20.

⁹⁹ Paccès (2022) Supply Chain Liability in the Corporate Sustainability Due Diligence Directive Proposal, the ECGI Blog.

¹⁰⁰ Lafarre (2022) Mandatory Corporate Sustainability Due Diligence in Europe: The Way Forward, the ECGI Blog.

Established business relationships

As established, one of the goals of the CSDDD proposal is to lead companies to create a HREDD policy and framework and apply them to their value chain. To this effect, the Directive prescribes that a company's due diligence obligations shall extend to adverse impact at the level of its own operations, the operations of its subsidiaries and, importantly, their broader supply chains, to the extent that they consist of an 'established business relationship'. This formulation, that recurs throughout the CSDDD proposal, including in Articles 5 through 10, has been discussed extensively.¹⁰¹ Article 3(f) provides a definition of 'established business relationship' which recites as follows:

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

In this sense, a company's HREDD obligations apply to adverse impact at the level of its 'lasting' and more stable business relationships, both upstream (i.e. suppliers, manufacturers, transporters etc.) and downstream (i.e. distributors, retailers, buyers etc.).¹⁰² The commentary on the use of this formulation in the context of the HREDD formulation has been focused on different points. A first consideration is that the concept of 'established business relationships' is not sufficiently defined by the Directive, and it is not necessarily clear what 'lasting' means for the purpose of a relationship being classified as 'established'. Additional clarifications in the text specify that 'indirect relationships' can fall under this scope as well, but there still is much room for divergent interpretations of these articles.¹⁰³ Another important point is that this approach does not necessarily follow the one established in the UNGPs.¹⁰⁴ The Principles, in fact, take a 'risk-based approach' in which companies focus action on the most salient human rights or environmental issues wherever in their value chain they occur, on the basis of an ongoing risk assessment. The UNGPs also take a broader approach to 'business relationships'.¹⁰⁵ Essentially, the difference lies in the fact that the Principles prescribe that companies should be responsible to conduct HREDD with respect to all entities in their value chain, based on the severity of impact rather than the nature of the business relationship, whereas the 'established' qualifier in the CSDDD proposal is more restrictive. In addition to be materially different from these existing standards, it has been noted that the proposed Directive's approach in this regard is a departure from existing best practices.¹⁰⁶ Reportedly, certain companies – especially some of the larger companies that will fall in the personal scope of the Directive – already undertake due diligence with respect to their value chain, beyond the given definition of established business relationships.¹⁰⁷

According to commentators, this approach could have two negative effects: firstly, adding the qualifier will raise the threshold for access to remedy, as it makes it increasingly hard for victims to benefit from the civil liability mechanism.¹⁰⁸ Secondly, this could create perverse incentives, by which companies could structure their value chains in such a way as to avoid engaging in 'established' business relationships with high-risk entities or in high-risk countries. The risk being that companies will hop from one contractor and supplier to another and keep them at arm's length, rather than engaging long-term and seeking to improve their human

¹⁰¹ Lafarre (2022) Mandatory Corporate Sustainability Due Diligence in Europe: The Way Forward, the ECGI Blog; Holly & Andreasen Lysgaard (2022) Legislating for impact: analysis of the proposed EU Corporate Sustainability Due Diligence Directive p. 14-17.

¹⁰² Lapr vot  et al. (2022) Altert Memorandum, The Corporate Sustainability Due Diligence Directive, Clearly Gottlieb

¹⁰³ See: CSDDD proposal Recital 20 p.33.

¹⁰⁴ Lafarre (2022) Mandatory Corporate Sustainability Due Diligence in Europe: The Way Forward, the ECGI Blog; Shift (2022) The EU Commission's Proposal for a Corporate Sustainability Due Diligence Directive – Shift's Analysis p. 4-5.

¹⁰⁵ UNGPs, Commentary to Principle 13: "A and its "business relationships" are understood to include relationships with business partners, entities in its value chain, and any other non-State or State entity directly linked to its business operations, products or services" p. 15.

¹⁰⁶ Lafarre (2022) Mandatory Corporate Sustainability Due Diligence in Europe: The Way Forward, the ECGI Blog.

¹⁰⁷ Shift (2022) The EU Commission's Proposal for a Corporate Sustainability Due Diligence Directive – Shift's Analysis p.5

¹⁰⁸ Id. Ibid. 16.

rights and environmental performances.¹⁰⁹ This point proves particularly problematic with respect to the CSDDD proposal's relationship to the UNGPs, as one of the core tenants of the Principles is that companies should leverage their business connection to enact real change.¹¹⁰ In addition, short or informal business relationships are those that present the highest risks for adverse impacts and that companies may well be able to exercise their influence in such situations as well.

Contractual Assurances

Another contested point regarding the HREDD obligation is the Directive's reference to 'contractual assurances' in Articles 7 and 8 as one of the tools at the disposal of companies to establish and ensure compliance across its value chain and to a larger extent discharge its own due diligence obligation. This means that companies are encouraged to include in contracts with suppliers, contractors and such, a clause that ensures that said supplier or contractor will comply with the main company's HREDD policy or code of conduct and cascade requirements further up or down the value chain. This approach clearly seeks to leverage the contractual control that large companies can exercise on entities that work with and for them. This, on its face, seems to align with the overall goals of the CSDDD proposal and even with the UNGPs, as to the emphasis on leverage. However, attention has been brought to the fact that allowing for such contractual guarantees may lead to box-ticking, paper-based compliance and enable companies to escape liability by shifting responsibility away from them, along the value chain.¹¹¹ This reduces the impact of the HREDD obligation and fails to incentivise structural changes in the company's practices. In addition, the proposed Directive's dependency on contractual assurances risks diverting attention away from the wider set of tools that companies can actively employ in order to exercise their leverage on third parties like training within their value chains, adjusting their own pricing and purchasing practices if these are found to exacerbate risks further down the supply chain, or even cooperating with regional governments on the implementation of protective effective legislation.

It should be pointed out that the Commission is yet to provide a model contractual clause that, according to Article 12, would provide more clarity and guidance to this effect.¹¹² However, it has been noted that contractual assurances and social audits have historically proven ineffective in similar scenarios.¹¹³ As mentioned in a previous subsection, this approach too has been flagged as potentially creating perverse incentives, leading companies to step back from already established best practices.¹¹⁴ Ultimately, the co-legislators may want to consider more effective options and put a higher emphasis on the general duty to identify, prevent, and bring to an end adverse impact, and minimise the role of specific measures such as 'contractual assurances', which might be used as complementary tools.

Stakeholder Engagement

As a final note on the material scope of the proposal, it should be pointed out that the proposed Directive makes reference to stakeholder engagement. In Articles 6, 7 and 8 the CSDDD proposal states that, 'where relevant', companies shall seek the consultation of stakeholders in order to: gather information on actual or

¹⁰⁹ Id. Ibid.

¹¹⁰ See: UNGPs Principle 19 and commentary p.20-22.

¹¹¹ Lafarre (2022) Mandatory Corporate Sustainability Due Diligence in Europe: The Way Forward, the ECGI Blog; Holly & Andreasen Lysgaard (2022) Legislating for impact: analysis of the proposes EU Corporate Sustainability Due Diligence Directive p. 19.

¹¹² CSDDD proposal Article 22.

¹¹³ Lafarre (2022) Mandatory Corporate Sustainability Due Diligence in Europe: The Way Forward, the ECGI Blog.

¹¹⁴ Holly & Andreasen Lysgaard (2022) Legislating for impact: analysis of the proposes EU Corporate Sustainability Due Diligence Directive p. 20.

potential adverse impacts (CSDDD proposal Article 6); develop a prevention action plan (CSDDD proposal Article 7); and develop a corrective action plan (CSDDD proposal Article 8). According to the Directive, ‘stakeholders’ include employees and other individuals, groups, communities, or entities potentially affected by the business operation of a company and its value chain.¹¹⁵

Although it is ultimately positive for the CSDDD proposal to encourage stakeholder engagement, the qualifier ‘where relevant’ significantly diminishes the effectiveness of these provisions, as the decision on whether to consult stakeholders at all is left to the discretion of companies in all cases.¹¹⁶ In order to foster meaningful stakeholder engagement and ensure that companies conduct proper, people-centric impact assessments and action plans, the role of stakeholders should be expanded and strengthened.¹¹⁷

LITIGATION RISK: CIVIL LIABILITY FOR THE COMPANY

As mentioned above, the CSDDD proposal establishes a civil liability mechanism for potential victims of human rights or environmental harms, resulted from a violation of the obligations established by the Directive.¹¹⁸ Civil liability is covered by Article 22 of the proposed Directive. According to Article 22 paragraph 1, the civil liability regime is applicable to companies which fail to comply with Articles 7 and 8 of the Directive. Specifically, the company is liable in situations in which that failure has resulted in an adverse human rights or environmental impact and caused damage. Article 22 paragraph 2 further entrenches the ‘reasonableness test’ (see subsection on ‘appropriate measures’), by stating that a company should not be liable under paragraph 1 unless its actions were unreasonable.¹¹⁹

It appears that, with this set of articles, the Commission has tried to strike a balance between ensuring access to remedy for potential victims of human rights and environmental harms and mitigating the litigation risk faced by companies. Whether this balance has been struck fairly depends on the point of view of the commentator.¹²⁰ Some have pointed out how the ‘reasonableness test’, paired with the formulation ‘appropriate measures’ in Articles 7 and 8, the ‘contractual assurances’ caveat and the ‘established business relationship’ qualifier,¹²¹ creates an excessively high onus on victims, limiting their ability to obtain compensation for their losses.¹²² This point is particularly exacerbated when considering the issue of the burden of proof that, as mentioned before, has not been reversed.¹²³ Although the proposal puts forward “this fault-based liability regime,” the burden of proof is ultimately regulated in the national laws of the Member States.¹²⁴ As previously mentioned, most EU legal systems put the burden on the claimant to prove a large variety of facts, including: the violation of human right or environmental standards, the harm suffered

¹¹⁵ CSDDD proposal Article 3(n).

¹¹⁶ O'Brien (2022) Sustainable corporate governance: submission to Consultation on European Commission's proposal for a Directive on corporate sustainability due diligence COM(2022)71 final p.14.

¹¹⁷ Article One (2022) EU Commission Proposal–Corporate Sustainability Due Diligence Directive, Briefing Note No. 2 p.7; European Coalition for Corporate Justice (2022) *European Commission's proposal for a directive on Corporate Sustainability Due Diligence A comprehensive analysis*, Legal Brief p.17.

¹¹⁸ See: CSDDD proposal Articles 9 and 22.

¹¹⁹ CSDDD proposal Article 22(2).

¹²⁰ For example, perhaps surprisingly, CSDDD proposal's civil liability provisions have even been supported by exponents of the business community. See: Business & Human Rights Resource Centre (2022) Selected responses to EU Commission's proposal for a directive on Corporate Sustainability Due Diligence.

¹²¹ According to commentators, this also contradicts the UNGPs – especially Principle 17 – which states that companies should carry out due diligent with respect to any entity to which it is ‘directly linked’, not only with which it has an ‘established business relationship’. See: Lafarre (2022) Mandatory Corporate Sustainability Due Diligence in Europe: The Way Forward, the ECGI Blog.

¹²² Holly & Andreassen Lysgaard (2022) Legislating for impact: analysis of the proposes EU Corporate Sustainability Due Diligence Directive p. 22.

¹²³ O'Brien (2022) Sustainable corporate governance: submission to Consultation on European Commission's proposal for a Directive on corporate sustainability due diligence COM(2022)71 final p.17-18. Paccès (2022) Supply Chain Liability in the Corporate Sustainability Due Diligence Directive Proposal, the ECGI Blog.

¹²⁴ CSDDD proposal Recital 58 p.43. On the CSDDD and applicable law see also: Dias (2022) *CSDD and PIL: Some Remarks on the Directive Proposal*, Conflict of Laws.net.

by the victim, the causal link between them, and possibly even whether the company has breached its HREDD duty. All of which is extremely hard for any victim to prove, especially considering the lack of access to internal corporate information.¹²⁵

Regulating the burden of proof, as well as establishing a causal link between liability and harm, is a major challenge which the CSDDD proposal avoids by delegating it to the Member States' national laws.¹²⁶ Ideally, the Directive itself should ensure a fair distribution of the burden of proof, as well as ensuring that companies are not able to unduly escape liability (i.e. through 'contractual assurances' or by seeking third-party auditing to verify compliance).¹²⁷ In addition, the Directive should address the barriers to justice often faced by victims of human rights and environmental abuses (such as the limitation period for bringing liability claims, collective redress mechanisms, enabling civil society organisations and trade unions to bring actions on behalf of victims and ensuring that Member States provide support to claimants).¹²⁸ Other points raised by commentators are that civil liability should not be restricted to preventing or bringing to an end potential harm, but should also be established for failures to comply with other articles of the Directive; that civil liability for third-party auditors should be clarified; and that the proposal should also include the possibility to request that courts issue injunctive relief i.e. order companies to act or to refrain from acting in a certain way with the aim of preventing harm or an infringement of due diligence requirements.

A different point of view relates to the fact that, in the CSDDD proposal, liability is provided not only for harms that were identified and should have been brought to an end (Article 8), but also for harms that should have reasonably been foreseen (Article 7). As such, the scope of liability covered by Article 22 could already be considered quite broad. Given the vagueness of the formulations it is expected that much regarding the strength and fairness of the civil liability mechanism will come down to the practical application of these provisions by the courts. It should also be noted that the Commission put in place incentives for companies to invest in sustainability in Articles 20-22, as it is stated that liability can potentially be reduced on the basis of the company's efforts to cooperate with the enforcement authorities and to comply with HREDD.¹²⁹

Multiple commentators have also noted that the scope of the HREDD obligation, as in the director's responsibility to implement and oversee the HREDD policy, ought to be separated from the scope of civil liability.¹³⁰ Currently, the Directive foresees the same scope for *civil liability* as the scope of the *due diligence duty*, resulting in the civil liability scope being quite broad. To address this issue and to narrow the scope of civil liability, the due diligence duty itself is then limited by the abovementioned qualifier 'established business relationships'. Although this compromise evidently seeks to strike a balance and diminish the litigation risk for the company, this choice comes with the several issues explained above in the previous sub-section on 'established business relationships'. It is to avoid these hurdles and to allow the due diligence duty to conform to the wider standard of the UNGPs, that commentators have recommended this separation from the scope of civil liability.¹³¹ On the other hand, this reduces the role of an effective civil liability mechanism to

¹²⁵ European Parliament (2022) Corporate sustainability due diligence: Could value chains integrate human rights and environmental concerns? p. 20.

¹²⁶ O'Brien (2022) Sustainable corporate governance: submission to Consultation on European Commission's proposal for a Directive on corporate sustainability due diligence COM(2022)71 final p.18.

¹²⁷ It should be pointed out that, notably, certain commentators have made the exact opposite prescription, invoking that the burden of proof should be strictly kept on the victim. See for example Insurance Europe (2022) Response to EC CSDD Directive proposal p. 4.

¹²⁸ ICBHR (2022) How do we improve the EU Corporate Sustainability Due Diligence law? Briefing Paper p.6; European Coalition for Corporate Justice (2022) European Commission's proposal for a directive on Corporate Sustainability Due Diligence A comprehensive analysis, Legal Brief p. 4.

¹²⁹ See CSDDD proposal Article 20-22. See Also ECGI (2022) Online Policy Workshop - European Commission Directive on Corporate Sustainability Due Diligence, Day 2, 1st Speaker, John Armour.

¹³⁰ Davis (2022) Remarks by Shift's VP, Rachel Davis at the event "EU Human Rights and Environmental Due Diligence in Global Value Chains", hosted by the EU Parliament Working Group on Responsible Business Conduct; ECGI (2022) Online Policy Workshop - European Commission Directive on Corporate Sustainability Due Diligence, Day 1, 3rd Speaker, Anne Lafarre.

¹³¹ Shift (2022) The EU Commission's Proposal for a Corporate Sustainability Due Diligence Directive - Shift's Analysis p. 4.

incentivise appropriate due diligence across the whole value chain; there may also be other criteria to determine levels of responsibility and liability.¹³²

As mentioned, Article 22 establishes civil liability on companies, not on directors. Conversely, directors are addressed by CSDDD proposal Articles 25 and 26 respectively covering the director's duty of care and their duty to oversee due diligence. These two aspects will be addressed by the next main section, as well as a continuation of the assessment of the 'litigation risk' implications.



LITIGATION RISK: PERSONAL LIABILITY FOR DIRECTORS AND THE DUTY OF CARE

CSDDD proposal Article 25, cited below, establishes a broad duty of care for directors of companies under the scope of application of the Directive:

Article 25

Directors' duty of care

- 1. Member States shall ensure that, when fulfilling their duty to act in the best interest of the company, directors of companies referred to in Article 2(1) take into account the consequences of their decisions for sustainability matters, including, where applicable, human rights, climate change and environmental consequences, including in the short, medium and long term.*
- 2. Member States shall ensure that their laws, regulations and administrative provisions providing for a breach of directors' duties apply also to the provisions of this Article.*

According to this formulation, directors, while fulfilling their duty to act in the best interest of the company, should also consider the implications on human rights, the environment and sustainability in general. Accordingly, failing to do so would trigger the Member States' national laws on breach of director's duties.

A few key considerations can be made on this article: firstly, it is interesting that the Commission is seeking to harmonise the duty of care of directors – relative to sustainability concerns – at EU level, and seemingly doing so following the blueprint on international soft law on business and human rights.¹³³ By enshrining such language in EU hard law, the CSDDD proposal could end up broadening the concept of 'corporate purpose' and steer the Member States' legal systems towards a more 'pluralist' or 'stakeholder'-oriented approach to company value creation.¹³⁴ Secondly, as it has been mentioned in the first part of this article, Article 25 seems to have taken considerable inspiration from Section 172 of the UK Companies Act,¹³⁵ also

¹³² For example the UNGPs' "cause, contribute, linkage" concept can be used to establish levels of liability proportional to different levels of responsibility that a company may have incurred in, depending on whether it has caused, contributed to or is directly linked to adverse impacts. See: UNGPs Principles 13 and 17. See also: Business & Human Rights Resource Centre (2020) Key Considerations for Effective Mandatory Due Diligence Legislation.

¹³³ O'Brien (2022) Sustainable corporate governance: submission to Consultation on European Commission's proposal for a Directive on corporate sustainability due diligence COM(2022)71 final p.18.

¹³⁴ For a nuanced and innovative perspective on corporate purpose and stakeholder language in the European legal systems see: Sjøfjell & Mähönen (2022) Corporate purpose and the misleading shareholder vs stakeholder dichotomy, University of Oslo Faculty of Law Legal Studies Research Paper Series No. 2022-43.

¹³⁵ ECGI (2022) Online Policy Workshop – European Commission Directive on Corporate Sustainability Due Diligence, Day 2, Q&A section.

known as the cornerstone of the 'enlightened shareholder model'. Much like Section 172,¹³⁶ CSDDD proposal Article 25 consists of an *ex ante* procedural obligation expressed as a duty of good faith which is ultimately protected by the standard of the 'business judgment rule'.¹³⁷ The similarity with the UK law should enhance legal predictability and ease the worries of enhanced litigation risk or personal liability risks for directors, as Article 25 can be expected to be applied in a similar way as Section 172 has been, for the last 16 years. Despite the similarity with section 172 Companies Act, it should be pointed out that Article 25 remains quite significantly vaguer than the UK law.¹³⁸ A feature that critics have attributed to lobbying,¹³⁹ and that could hinder the overall effectiveness of the provision, as well as diminish legal predictability. Ultimately, should the Commission wish to keep pace with the increasing pressure of stakeholders and institutional investors and the growing importance of sustainable finance, Article 25 ought to be reinforced and director's duties clarified.¹⁴⁰ The strengthening of this aspect would also benefit from a greater emphasis on the need for companies to adopt an overarching corporate purpose rooted in the pursuit of sustainable value creation.¹⁴¹

When considering the proposed Directive's impact on litigation risk and the case of director's personal liability, Article 25 should be looked at in junction with Article 26. CSDDD Article 26 establishes that directors shall be responsible for overseeing the implementation and monitoring of the HREDD policy and that, in doing so, they take into account human rights and environmental adverse impacts in accordance with Articles 6, 7, 8 and 9 of the Directive. Effectively, the link between the HREDD obligations and director's responsibility in Article 26 reinforces the due diligence approach and encourages the awareness and consideration of human rights and environmental impacts in the company's governance at large, rather than it being limited to dedicated compliance departments. Commentators have pointed out that Article 26 could further emphasise the obligation to oversee the due diligence policy, as well as provide more indications on how exactly directors should carry out their duties within the company.¹⁴²

CSDDD proposal Articles 25 and 26 have sparked some criticism from some business actors related to the risks that could come with heightening the personal liability of directors. A concern is that the vagueness of the proposal's measures in this regard may increase mistrust in directors and impede them from carrying out their functions: taking business risks and freely exercising business judgement.¹⁴³ In particular, there has

¹³⁶ Companies Act (2006) Section 172, Duty to promote the success of the company.

¹³⁷ "The Business Judgment Rule is a legal doctrine that helps to guard a corporation's board of directors (B of D) against frivolous legal allegations about the way it conducts business. A legal staple in common law countries, the rule states that boards are presumed to act in 'good faith' [...] [Investopedia. Laws and regulations. Business Judgment Rule.](#)

¹³⁸ Section 172 of the Companies Act goes into detail as to what defines the director's duty to act in 'good faith' and, in particular, it provides a comprehensive list of all the long-term interests that a director should take into account (i.e. employees; business relationships with suppliers, customers and others; the company's operations' impact on the environment; the company's reputation etc.). It also provides for a hierarchy of interests (i.e. ultimately shareholder interests prevail, but stakeholder interests should be considered as much as possible) and refer to corporate purpose. Overall, the article is much more structure and detailed than CSDDD proposal Article 25. For reference, see: Companies Act (2006) Section 172, Duty to promote the success of the company.

¹³⁹ Lafarre (2022) Mandatory Corporate Sustainability Due Diligence in Europe: The Way Forward, the ECGI Blog.

¹⁴⁰ It should be noted that some commentators have taken the opposite stance on Article 25 and the director's duty of care, suggesting that the article should be out-right deleted from the CSDDD proposal. For different perspectives on this point see: ECLE (2022) The proposed Due Diligence Directive should not cover the general care of directors, the ECGI Blog; Business Europe (2022) Corporate Sustainability Due Diligence proposal, Comments Paper.

¹⁴¹ A stronger iteration of the director's duty of care, paired with a defined corporate purpose, could facilitate the integration of sustainable value creation not only with respect to HREDD, but into all facets of a company's business model and overall strategy. Sjäffjell & Mähönen (2022) Corporate purpose and the misleading shareholder vs stakeholder dichotomy, University of Oslo Faculty of Law Legal Studies Research Paper Series No. 2022-43 p.19.

¹⁴² Some examples and suggestions to this effect are: the article could assign a more proactive role to the board, as well as specify the regularity with which reports should be submitted to the boards; directors could be more specifically held responsible for approving and implementing transition and sustainability plans, including science-based targets, as well as adapting the business model and strategy accordingly; climate-related obligations could be explicitly included in directors' duties, rather than being part of the company's obligations; higher emphasis could be put on double materiality with respect to impact and risk assessments; etc. On this topic see also: Sjäffjell & Mähönen (2022) Corporate purpose and the misleading shareholder vs stakeholder dichotomy, University of Oslo Faculty of Law Legal Studies Research Paper Series No. 2022-43 p.25.

¹⁴³ On a 'director's perspective' on the CSDDD proposal see: ECGI (2022) Online Policy Workshop - European Commission Directive on Corporate Sustainability Due Diligence, Day 2, 5th Speaker, Daniela Weber-Ray.

been commentary expressing that the CSDDD proposal’s material scope may be too ambitious and lead to an excessive amount of internal procedure within companies and supply chains.¹⁴⁴ This, paired with the reservations relating to civil and personal liability laid out above, ties in with the overregulation concerns addressed at the very beginning of this article. Others have since long pointed out that due diligence is more than a mechanical process, “but one that lives and breathes, informing company behaviour and decision-making”.

Having noted some of the criticism on liability and litigation risks with relation to CSDDD proposal Articles 25 and 26, one last clarification should be highlighted. Director’s duties – be it the duty of care or the duty to supervise the due diligence policy – are owed to the *company*.¹⁴⁵ As such, they are only enforceable by the company’s shareholders against a director, and they are only enforceable if it can be shown that a director’s failure to comply with said duties has generate a loss for the company. In the case of CSDDD proposal Article 25 and 26, the shareholders would have to prove that a director’s failure to appropriately consider human rights or environmental concern in their operations, or their failure to appropriately supervise the HREDD policy, has directly caused a loss to the company. Unsurprisingly, establishing such causation could prove very challenging.¹⁴⁶



The following – and final – main section on the overall assessment of the proposed Directive’s provisions, addresses the topic of executive remuneration.

EXECUTIVE REMUNERATION

Outside of the provisions on HREDD and liability, the CSDDD proposal also addresses the topic of executive remuneration. CSDDD proposal Article 15(3) provides indications relating to how the compensation of the directors of relevant companies shall be calculated, when considering certain obligations provided in Article 15(1) and (2). Specifically, Article 15 provides obligations relating to climate change, and references their relation to the *variable* component of executive remuneration.¹⁴⁷ CSDDD proposal Article 15 recites:

Article 15
Combating climate change

1. Member States shall ensure that companies referred to in Article 2(1), point (a), and Article 2(2), point (a), shall 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

¹⁴⁴ ECGI (2022) Online Policy Workshop - European Commission Directive on Corporate Sustainability Due Diligence, Day 2, 5th Speaker, Daniela Weber-Ray.

¹⁴⁵ This is especially true in common law jurisdictions. See: [To whom are directors' duties owed?](#)

¹⁴⁶ ECGI (2022) Online Policy Workshop - European Commission Directive on Corporate Sustainability Due Diligence, Day 2, 1st Speaker, John Armour.

¹⁴⁷ Typically, a corporate director’s compensation is divided in a ‘fixed’ salary (i.e. a specific pre-determined) and ‘variable component’ (i.e. part of the compensation is calculated based on certain variables, the performance on the director over a given period of time or the achievement of pre-set goals or targets). The variable component of remuneration can be used to influence the behaviour of directors and financially incentivize them to pursue the company’s financial or non-financial goals. As such, variable remuneration based on sustainability metrics can be used to foster sustainable corporate governance. For more information see: Reward Value Foundation (2020) Green Paper - Reward Value.

reasonably available to the company, the extent to which climate change is a risk for, or an impact of, the company's operations.

2. Member States shall ensure that, in case climate change is or should have been identified as a principal risk for, or a principal impact of, the company's operations, the company includes emission reduction objectives in its plan.

3. Member States shall ensure that companies duly take into account the fulfilment of the obligations referred to in paragraphs 1 and 2 when setting variable remuneration, if variable remuneration is linked to the contribution of a director to the company's business strategy and long-term interests and sustainability.

As explained in the main section on 'scope of application', the Directive imposes different obligations on different types of companies. In this case, Article 15 only applies to 'group 1 companies' (i.e. large EU and non-EU-based companies).¹⁴⁸ In itself, this choice already raises concerns, since it appears hard to understand why the 'high-risk sector SMEs' of group 2 should be excluded by a provision on climate change. Generally, Article 15 appears as establishing a procedural obligation to 'group 1' companies to establish and implement a plan aimed at addressing their impact on climate change, with particular reference to the Paris Agreement (and its 1.5° C metric) and emission reduction. In paragraph 3, the proposed Directive makes reference to variable remuneration as a way to incentivise directors to consider the company's long-term interests and sustainability in the fulfilment of this obligation.

A few annotations can be made on this article. Firstly, it appears that the concept of 'sustainable' executive remuneration has been applied very narrowly: the wording of paragraph 3 explicitly links 'variable remuneration' to the obligations referred to in the paragraphs 1 and 2, which are entirely centred on the topic of climate change, and specifically refer to the '1.5°C metric' of the Paris Agreement. Notably, emission reduction is not even included in the Annex listing the environmental impacts subject to the HREDD duty. Although the reference to 'transition to a sustainable economy' in paragraph 1 could be interpreted as broadening the scope of the article to other sustainability factors (notably 'sustainability' or 'sustainable economy' are not defined by the Directive), the sections of the Explanatory Memorandum dedicated to Article 15 seem to confirm the intention of limiting its scope to climate change and emission reduction.¹⁴⁹ In addition, the wording of paragraph 3 restricts the relevance of sustainable remuneration even further, by implying that companies should take into account these environmental parameters *only if and when* variable remuneration *is linked* to 'the contribution of a director to the company's business strategy and long-term interests and sustainability'. Effectively, paragraph 3 of Article 15 applies on a strictly non-binding and voluntary basis and the fact that sustainable remuneration is not at all linked to Article 25 and 26 creates an accountability gap. In addition to failing to lay the foundation for companies to develop comprehensive remuneration policies, Article 15 fails to properly address climate change. To fully comply with UN and OECD standards, the Directive should establish an obligation to adopt and implement an effective transition plan

¹⁴⁸ "Member States shall ensure that companies referred to in Article 2(1), point (a), and Article 2(2), point (a) [...] CSDDD proposal Article 15.

¹⁴⁹ "(50) In order to ensure that this Directive effectively contributes to combating climate change, 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. In case climate is or should have been identified as a principal risk for or a principal impact of the company's operations, the company should include emissions reduction objectives in its plan.

(51) With a view to ensure that such emission reduction plan is properly implemented and embedded in the financial incentives of directors, the plan should be duly taken into account when setting directors' variable remuneration, if variable remuneration is linked to the contribution of a director to the company's business strategy and long-term interests and sustainability." CSDDD proposal, Explanatory Memorandum p. 41.

including timebound reduction targets, that accounts for both direct and indirect emissions,¹⁵⁰ and include climate change impacts in the due diligence duty by extending the Annex accordingly.

Ultimately, it is easy to see how the effectiveness of Article 15 – and in particular paragraph 3 – leaves much to be desired, especially considering the larger ambitions for sustainable reform originally attributed to the Sustainable Corporate Governance Initiative. This issue ties into a broader point on the Directive’s relationship to sustainability in general and its approach to the regulation of sustainability in corporate governance. This aspect, as it relates to remuneration and to other key points, will be addressed in greater depth in the second part of this article on ‘considerations’. As such, the following sections will comment on the original intentions behind the CSDDD proposal, how the development of the proposal has related to them and elaborate on broad assessments of the Directive’s conceptualization of sustainability.

PART 2 – CONSIDERATIONS

The CSDDD proposal has been an important step towards the construction and harmonisation of a European framework for sustainable governance. By creating the basis for a unified understanding of HREDD and director’s duties as relating to sustainability at EU level, the Commission has achieved an important milestone. As it stands now, the proposed CSDDD is still imperfect and, as mentioned throughout this article, received a critical reaction from commentators across the board. This first wave of criticism, in some ways, reflects the sense of disappointment and unfulfilled expectations from various stakeholders that had put faith in the Proposal to comprehensively address many different issues. However, it is important to remember that the proposed Directive is still unfinished and undergoing the legislative process. This text, albeit imperfect, is ultimately a jumping-off point that can be used to define and refine new and better solutions. In addition, it is important to note that the CSDDD proposal is a product of compromise and careful consideration of many different opinions and points of views.¹⁵¹ Indeed, even the criticism received by the proposed Directive has stemmed from a variety of policy perspectives,¹⁵² with commentators advocating for recommendations and advice contradictory to those presented in this article.¹⁵³ It is also not the case that the calls for a harder, more far-reaching approach have exclusively come from non-governmental organisations and academics, and that invocations for less stringent provisions have solely come from market actors and the business community. Overall, the types of criticism and their sources have been widely varied.¹⁵⁴

It is ultimately up to the co-legislators to balance conflicting interests and find the most workable solutions, considering the ultimate goals and intentions behind this initiative. It is in this light and with this spirit, that

¹⁵⁰ Notably, some commentators have criticised Article 15 for the opposite reason, maintaining that the CSDDD proposal should refrain from addressing climate change at all. For a critical perspective of the inclusion of this metric in particular, and climate change in general in the CSDDD proposal see: ECLE (2022) Why Article 15 (combating climate change) should be taken out of the CSDD, the ECGI Blog.

¹⁵¹ “In total, 473.461 public responses were obtained during the consultation period. In addition, currently 149 position papers were received outside of the EU Survey.” European Commission (2021) Sustainable corporate governance initiative: Summary report – public consultation p.2.

¹⁵² Examples of commentary not yet cited in this article from individuals and organizations holding different perspectives and using different policy lenses are: UNICEF (2022) An EU Corporate Sustainability Due Diligence Directive that Works for Children UNICEF comments on the European Commission proposal [COM(2022) 71 final]; FERMA (2022) FERMA position paper on the European Commission’s proposal for a Corporate Sustainability Due Diligence Directive (CSDD), Position Paper; Lidman (2022) The role of corporate governance in sustainability and why the Commission’s CSDDD proposal might do more harm than good, the ECGI Blog.

¹⁵³ A notable example is the position paper from a group of Nordic and Baltic company law scholars, heavily criticising the CSDDD’s efforts to regulate aspects of corporate governance. This paper, in turn, has been itself criticised by Sjøfjell and Mähönen, who align more with the policy perspective taken by Reward Value. For more information on both see: Andersen et. Al (2022) Response to the Proposal for a Directive on Corporate Sustainability Due Diligence by Nordic and Baltic Company Law Scholars, Nordic & European Company Law Working Paper No. 22-01; and Sjøfjell & Mähönen (2022) Corporate purpose and the misleading shareholder vs stakeholder dichotomy, University of Oslo Faculty of Law Legal Studies Research Paper Series No. 2022-43.

¹⁵⁴ For examples of ‘business actors’ calling for a more stringent approach in selected areas see: Business & Human Rights Resource Centre (2022) Selected responses to EU Commission’s proposal for a directive on Corporate Sustainability Due Diligence; and Business & Human Rights Resource Centre (2022) More than 100 companies and investors call for effective EU corporate accountability legislation.

the second half of this article remarks on the most pressing considerations and key points of interest and comment on Reward Value's perspective on the CSDDD proposal. Having the vantage point of being a think tank specialising in sustainable executive remuneration and having actively participated to the Commission's consultations for the proposed Directive in this regard, the following sections will mainly focus on the Directive's conceptualisation of sustainability, topics such as the 'time horizon element' of corporate governance, ESG metrics and their relevance and the opportunities thereof as they relate to potential improvements of the CSDDD proposal's text.

AN UNBALANCED APPROACH TO SUSTAINABILITY

Other than the more specific technical and legal issues raised in the previous sections, which might be addressed by the co-legislators during the next phase of the legislative process, one may notice a shift of attitude of the Commission from the beginning phases of the conceptualisation of the CSDDD to the actual drafting of the text of the Directive. More specifically, one could say that, during the consultation and drafting process, the Commission seems to have lost a degree of ambition and confidence in the project and, eventually, scaled back on what were perceived as the original intentions of the Sustainable Corporate Governance Initiative.¹⁵⁵ The reasons for this shift in attitude can only be inferred by the circumstances and, ultimately, it is impossible to determine the exact factors that influenced the drafting process and how. Important insights can be gained by the Commission's summary report of the consultation's findings.¹⁵⁶ However, a likely factor is also attributable to the harsh negative backlash that followed the two foundational studies used by the Commission to prepare the consultation document that was used to poll stakeholders and other interested parties on how to draft the Directive. The two studies were strongly criticised, mostly on their methodology and conclusions regarding the issue of 'short-termism' in corporate governance.¹⁵⁷

One of the most noticeable consequences attributable to this backlash in the text of the Directive, is the unbalanced approach to the different elements of sustainability. Undoubtedly, HREDD is the topic most developed in the proposal, such as the finalised proposed Directive bares 'Corporate Sustainability Due Diligence' in the title. This is no surprise, given that legislative frameworks for HREDD have been developing across the EU in the past 6 years.¹⁵⁸ Other than on HREDD, which has also arguably been watered down compared to international standards, the Commission has arguably taken an even more cautious approach, and refrained from making bolder choices for the regulation of sustainability. This is particularly true with regard to the topics of sustainable executive remuneration, sustainability in the financial sector and sustainable corporate governance in general, which will all be addressed in greater detail in the following subsections. Indeed, outside of the articles pertaining to HREDD, the CSDDD proposal projects a level of adversity to the juxtaposition of corporate governance and 'sustainability' at large, preferring to keep a very narrow focus on specific environmental metrics.¹⁵⁹ The ambiguity and inconsistency in the Directive's approach to 'sustainability' is exacerbated by the fact that the concept of 'sustainability' itself is never defined in the text.

¹⁵⁵ E.g. see: European Commission (2021) Inception impact assessment - Ares(2020)4034032

¹⁵⁶ European Commission (2021) Sustainable corporate governance initiative: Summary report – public consultation, Directorate-General Justice and Consumers, Directorate A, Unit A3: Company law

¹⁵⁷ ECLE (2020) EC Corporate Governance Initiative Series: Comment by the European Company Law Experts Group on the European Commission's Consultation Document 'Proposal for an Initiative on Sustainable Corporate Governance'.

¹⁵⁸ See: Law No. 2017-399 (2017) *Loi de Vigilance* (France) and *Lieferkettensorgfaltspflichtengesetz*, BGBl I 2021, 2959 (Germany).

¹⁵⁹ Notably, even with respect to environmental issues, particular attention is given to the issue of climate change over other, equally relevant, aspects. Sjøfjell & Mähönen (2022) Corporate purpose and the misleading shareholder vs stakeholder dichotomy, University of Oslo Faculty of Law Legal Studies Research Paper Series No. 2022-43 p.23.

It is arguable that the backlash to the aforementioned studies could be the cause of this constrained approach, as the Commission was ultimately missing a strong academic justification to make prescriptions based on the assumptions that a 'short-term attitude' to corporate governance exists and is damaging to shareholders and stakeholders.¹⁶⁰ In addition, the possibility that other, more political influences such as lobbying could have played a role, cannot be ruled out. Whilst the Commission's change of attitude following the consultation period is understandable, the next subsections point out several points in which an overly cautious approach to key topics could hinder the Commission's ultimate goal to establish an actionable framework for sustainability and thereby miss out on an opportunity to pioneer the transition to a sustainable and inclusive economy.

THE MISSED OPPORTUNITY OF SUSTAINABLE EXECUTIVE REMUNERATION

As mentioned above in the review of Article 15, the concept of 'sustainable executive remuneration' is given very limited space in the text of the Directive. The only reference to 'variable remuneration' can be found in CSDDD proposal Article 15 and the relative paragraph of the Explanatory Memorandum.¹⁶¹ Even when remuneration is referred to in these two instances, it is carefully limited to one particular aspect of sustainability – i.e. climate change – and applicable in very specific circumstances.¹⁶² By taking this approach, the proposed Directive disconnects the concept of responsible executive remuneration from the broader interpretation of sustainability which includes human rights, governance, social factors and environmental concerns outside emissions reduction. This extremely narrow approach comes across as jarring, especially considering that these other sustainability metrics are represented in other parts of the Directive.¹⁶³ Ultimately, by addressing this issue in this way, the CSDDD proposal not only fails to establish a comprehensive framework for sustainable remuneration but it seems to have actively taken several steps backwards and, effectively, to have shut down any broader conceptualisation of sustainable executive compensation.

The lack of consideration for the topic of remuneration is problematic also because, when implemented, the proposed Directive is likely to have an impact on remuneration practices for Directors. For example, given the increased complexities, demands and elevated personal risk for directors in relation to Articles 25 and 26, it can be expected that board fee levels will increase. Had the proposed Directive more comprehensively addressed this topic, it could have provided for advice on how to handle these increases in a way that is consistent with its goals of fostering sustainable value creation. For example, directors pay should only increase in cases in which their personal reputation or finances are at risk. As such, directors should be denied the possibility to be compensated fully through insurance and maintain a minimum so-called 'own risk' in liability insurance policies. This prescription would support the degree of accountability of directors by making their level of remuneration conditional upon the personal financial impact of their duties. Additionally – or alternatively – the liability track record of directors could be monitored through a 'no-claim register', which could function as a quality indicator for directors. A high ranking on the liability register could warrant a higher director fee than a low ranking expressing a higher risk for stakeholders of insufficient board control. Ultimately, increased clarity on remuneration levels and the effects of directors' personal liability on

¹⁶⁰ For Reward Value Foundation's position on short-termism in corporate governance see: Reward Value Foundation (2021) Managerial and Capital Market Short Termism.

¹⁶¹ See: CSDDD proposal Article 15 Combating climate change and CSDDD proposal, Explanatory Memorandum p. 41.

¹⁶² "3. Member States shall ensure that companies duly take into account the fulfilment of the obligations referred to in paragraphs 1 and 2 when setting variable remuneration, if variable remuneration is linked to the contribution of a director to the company's business strategy and long-term interests and sustainability." CSDDD proposal Article 15.

¹⁶³ See: subsection on 'material scope' above.

pay would foster increased trust in the market, and reduce the uncertainty faced by board members, which could otherwise be steered away from high-risk managerial positions in companies falling under the personal scope of the CSDDD proposal.

Given the Commission's original ambitions to deliver a comprehensive sustainability framework for corporate governance and given the flourishing conversation on sustainable remuneration in this context,¹⁶⁴ this overly restrictive approach seems puzzling. Aside from the aforementioned criticism of the pre-consultation studies, some explanation could be found in the consultation findings.¹⁶⁵ Apparently, half of the consultation respondents avoided answering the question on 'mandatory sustainable remuneration measures', with companies and business associations being particularly reluctant to express an opinion.¹⁶⁶ It seems that the lukewarm response of market practitioners to the topic, might have led the Commission to refrain from taking a stronger stance on this topic. However, even considering this context, the active attempt to separate remuneration from broader sustainability factors like human rights, social welfare, and other environmental concerns feels like an unexpected outcome and insufficiently supportive of the purpose of the Directive. Limiting the relevance of executive remuneration to a single dimension of sustainability ultimately limits the possibility of establishing comprehensive and effective incentive structures for senior management. This disconnects executive pay from the pursuit of corporate purpose and broader responsible corporate behaviour, thus making it harder for companies to develop governance frameworks capable of fostering the desired level of care for sustainability.

MISSING THE TIME HORIZON ELEMENT

As mentioned above, the CSDDD proposal presents a somewhat hesitant approach to the concept of sustainability, which is left largely undefined. Similarly, the Directive fails to provide a strong framework for the 'temporal dimension' of sustainability. For something to be sustainable, it means that it should be able to be maintained and function in the long term. Although certain aspects of what 'sustainability' means in the corporate governance sphere are unclear and can be subject to debate (e.g. to what degree and which human rights and environmental concerns factor in a sustainable economy), the concept of 'long-term' is always fundamental. As such, the proposal makes frequent reference to 'long-term sustainable and responsible corporate behaviour' and more generally to the concept of long-term value creation. However, what 'long-term' means is never quite defined.

As explained above, the conceptualisation of the proposed Directive, as the consultation documents were first created, was heavily influenced by the idea of 'short-termism' in corporate governance and the need to correct this harmful trend. Expectedly, following the criticism and widespread challenges to that assumption, the Commission distinctly dropped and distanced themselves from any mention of short-termism. It seems that, perhaps due to the abovementioned circumstances, the Commission was ultimately not quite capable of establishing a strong enough framework for long-term value and how to achieve it. However, even considering this context, the temporal element of sustainability remains fundamental. Therefore, failing to establish guidelines or indications as to what 'long-term interests' or 'long-term value creation' is a clear missed opportunity.¹⁶⁷

¹⁶⁴ E.g. see: Reward Value Foundation (2020) Green Paper – Reward Value.

¹⁶⁵ European Commission (2021) Sustainable corporate governance initiative: Summary report – public consultation, Directorate-General Justice and Consumers, Directorate A, Unit A3: Company law.

¹⁶⁶ Id ibid. p. 8.

¹⁶⁷ For a closer look at Reward Value's position on long-term value creation please see: Reward Value Foundation (2022) Response to the Dutch Corporate Governance Code Proposal for Update.

MISSING THE ESG CONNECTION AND THE FINANCIAL SECTOR

Another thing that is interestingly missing from the CSDDD proposal is a reference to Environmental, Social and Governance (ESG) metrics, a widespread set of sustainability criteria predominantly used by companies to craft corporate policies and by financial actors to assess the sustainability of investments.¹⁶⁸ Indeed, ESG is not mentioned in the entire text of the Directive. Given the Directive's reliance of established international standards like the UNGPs, the absence of these metrics is striking, especially given that ESG have become increasingly popular and commonly used metrics in the realm of corporate governance and finance.¹⁶⁹ At the same time, there is increasing recognition of the need to regulate this area to avoid greenwashing, misleading metrics and overreliance on them, as well as strengthen the "S" in ESG.

Alongside the absence of ESG, the proposal notably pays limited attention to the sustainability of the financial sector in general, by limiting the applicability of the Directive to the very large – and few – financial undertakings covered by CSDDD proposal Article 2(1)(a).¹⁷⁰ Since the financial sector is not considered a 'high risk sector' all small, medium and 'midcap' size financial undertaking are automatically excluded.¹⁷¹ Moreover, as it is the case in other parts of the text, the Directive falls short of introducing appropriate obligations, since existing practices which are already carried out by mature financial institutions seem to exceed the CSDDD proposal's requirements.¹⁷² Finally, as pointed out by commentators, the Directive seems to have failed to take advantage of synergies with other EU legislation on sustainability in the financial sector, thus missing an opportunity to foster policy coherence and coordination within EU law.¹⁷³

FOOD FOR THOUGHT: REFRAMING SUSTAINABILITY

Following this broader analysis and commentary on the proposed CSDDD and its implications, this article seeks to conclude with one parting consideration.

The definition of sustainability and the delineation of a structured, consistent understanding of what it means for companies to be sustainable, are fundamentally important elements for policymaking in this field. Although sustainability is an inherently broad and all-encompassing thing, there is a pressing necessity for a guiding light and a clear path for regulators, stakeholders, and market participants to work with this concept in an actionable and coherent way. As evidenced from the criticism and considerations raised in this article and by many of the commentators referenced throughout, the lack of a sustainability definition and the inconsistent approach to the different elements of sustainability are the root of several concerns stemming from the text of the CSDDD proposal. While in the due diligence context, open terms such as "appropriate" are required to allow for context-sensitive solutions, vagueness and ambiguity in other regards harms legal predictability, increases uncertainty with respect to litigation risks and hinders policy coherence with other hard and soft law instruments.

One point that could be kept in mind going forward is the re-framing of sustainability under a more pointed and unified lens. As mentioned, sustainability is an inherently broad and dispersive concept, covering areas ranging from the fight against climate change, the conservation of natural resources, the preservation of

¹⁶⁸ See: [Investopedia, Environmental, Social, and Governance \(ESG\) Criteria](#).

¹⁶⁹ Reward Value Foundation (2020) Green Paper - Reward Value.

¹⁷⁰ Regulated financial undertakings fall under the definition of 'company' in CSDDD proposal Article 3(a)(iv).

¹⁷¹ Medium-size financial undertaking would not fall under the scope of CSDDD proposal Article 2(2)(a).

¹⁷² Shift (2022) The EU Commission's Proposal for a Corporate Sustainability Due Diligence Directive - Shift's Analysis p. 11; European Banking Federation (2022) EBF position paper on the Corporate Sustainability Due Diligence Directive (CSDD) p. 1.

¹⁷³ Holly & Andreassen Lysgaard (2022) Legislating for impact: analysis of the proposed EU Corporate Sustainability Due Diligence Directive p. 17-18.

local communities and the safety of their environment, the respect of workers' rights, social rights economic rights and fundamental human rights all over the world and more. Given the span of sustainability and the complex set of relationships and degrees of interactions that corporations can have with all of these different elements it is no wonder that the regulation of sustainability in corporate governance often results in a somewhat vague and unfocused approach. In light of this context, this article seeks to raise a point regarding re-framing sustainability around one single point of reference: humanity.

Too often in the sustainability discourse, human rights and environmental concerns are addressed separately and categorised in two different sections. Also common in corporate governance, is the tendency to focus on environmental metrics, which are more easily quantifiable, over human rights impacts and risks. Instruments like the proposed CSDDD in a way seek to overcome this gap by establishing inclusive frameworks like HREDD. However, the unbalanced way in which the different elements of sustainability have been addressed by the proposed Directive still show symptoms of this tendency. It should not be forgotten that environmental impacts and climate change are of great importance precisely because the climate crisis poses a direct danger on the human population and the ability of individuals to enjoy their fundamental human, social economic and cultural rights. Notwithstanding the reality that climate-induced migration, increasingly frequent natural disasters, and the fast depletion of natural resources are all factors that will contribute to inequality, social tensions and ultimately the destabilization of societies and economies on a global scale. Ultimately, as the environment is a human issue, and sustainability at its core is a human rights issue, something could be gained by re-centring the scattered landscape of sustainability around human rights.

CONCLUSIONS

As anticipated in our first response to the CSDDD proposal, Reward Value Foundation takes notes of the positive achievements of the proposed Directive and welcomes the steps towards a harmonised framework for sustainable corporate governance in Europe. After having analysed in depth the characteristics and implications of key article of the proposed Directive, this publication has highlighted several criticisms, areas of improvements and commented on the different facets of the decision-making process which led to the proposed Directive.

Throughout their communications and proposals, the European Commission has demonstrated their intention to become a leader and pioneer in the transition to a sustainable and inclusive economy and we wholeheartedly believe in the project for a sustainable European market. We also believe in the power of the European Union to wield its influence and spearhead a sustainable economic transition on a global scale. The CSDDD proposal represents an important step and plays a key role towards the achievement of these ambitions. It is for this reason that we invite the co-legislator to take advantage of the opportunities they are presented during the next phase of the legislative process and confidently embrace the full potential of the Corporate Sustainability Due Diligence Directive.

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