



The European Corporate Sustainability Due Diligence Directive: Ready or not, here I come

Introduction

On 23 February 2022, the European Commission published its much-anticipated proposal for a Corporate Sustainability Due Diligence (**CSDD**) Directive (**the Directive**).¹ In this briefing, we cover the essential features of the proposed Directive and what it could mean for businesses in Asia.

This briefing builds on and supplements our previous [Mandatory Human Rights Due Diligence Legislation Guidance for Suppliers Operating in Asia](#).

Background

Human rights due diligence (**HRDD**) is a cornerstone of the United Nations Guiding Principles on Business and Human Rights (**UNGPs**). HRDD involves:²

- Establishing procedures to identify actual and potential human rights impacts arising from a business' operations;
- Integrating and acting upon those findings to prevent potential human rights impacts, and mitigate actual human rights impacts that have occurred;
- Tracking the effectiveness of a business' responses to verify whether actual human rights impacts have been addressed;

- Communicating publicly how those impacts have been addressed; and
- Where a business has caused or contributed to adverse human rights impacts, it must also provide for effective remediation for affected persons and groups.³

Building on the UNGPs and other human rights instruments, some states have introduced 'anti-modern slavery' laws, including the UK's Modern Slavery Act 2015, the California Transparency in Supply Chains Act, and the New South Wales and Australian Federal Modern Slavery Acts. These laws – while significant – are not true HRDD laws as contemplated by the UNGPs. These laws generally do not require companies to conduct any due diligence or investigation into human rights abuses in their supply chains, or to ensure access to remedy for affected persons. Instead, they operate on a 'comply or explain' basis – requiring businesses to disclose what (if any) procedures they have in place to identify and address rights violations.

¹ European Commission (23 February 2022) Proposal for a Directive of the European Parliament and Council on Corporate Sustainability Due Diligence and amending Directive (EU) 2019/1937. 2022/0051 (COD). Available at: https://ec.europa.eu/info/sites/default/files/1_1_183885_prop_dir_susta_en.pdf

² UNGPs 17-21.

³ UNGP 22.

In more recent years, several EU Member States have introduced, or have announced plans to introduce, HRDD laws. These include France's *Loi relative au devoir de vigilance* (2017), and Germany's *Sorgfaltspflichtengesetz* (2021)⁴. These laws differ from modern slavery laws in that they cover a broad range of human rights violations, not just 'modern slavery', and impose specific obligations on companies to proactively investigate and address human rights abuses in their supply chains.

Building off these efforts, the proposed Directive represents a major step towards introducing legally binding standards on CSDD. If implemented, the Directive would establish the world's first binding international legal framework on CSDD and harmonise CSDD legislation across the EU.

What would the proposed Directive do?

The proposed Directive would impose obligations on relevant companies to conduct human rights and environmental due diligence.⁵ Among other things, this would require those companies to:

- Integrate due diligence into all their corporate policies and put in place a due diligence policy;⁶ Take appropriate measures to identify actual and potential adverse human rights and environmental impacts (HEIs) in their value chains;⁷
- Take appropriate measures to prevent potential HEIs that are or should have been identified. Where prevention is not possible or not immediately possible, take appropriate measures to adequately mitigate potential HEIs;⁸
- Take appropriate measures to bring actual HEIs that have been, or should have been, identified to an end. Where such actual HEIs cannot be brought to an end, companies must minimise the extent of their impact;⁹ and
- Establish complaints procedures accessible to persons affected by HEIs as well as trade unions, worker representatives, and civil society organisations.¹⁰

Large companies¹¹ must also adopt plans to ensure that the business model and strategy of the company are compatible with the transition to a sustainable economy and the limiting of global warming to 1.5°C in line with the Paris Agreement.¹²

⁴ The Netherlands has also introduced a more targeted child labour due diligence law - the *Wet zorgplicht kinderarbeid* 2019.

⁵ Directive, Article 4.

⁶ Directive, Article 5.

⁷ Directive, Article 6.

⁸ Directive, Article 7.

⁹ Directive, Article 8.

¹⁰ Directive, Article 9.

¹¹ I.e., companies incorporated inside or outside of the EU with a net annual turnover in the EU of at least EUR 150 million.

¹² Directive, Article 15.

The proposed Directive also adopts a range of measures to support companies' CSDD obligations:

- **Competent authority**

Each EU Member State must designate one or more supervisory authorities to supervise companies' compliance with their CSDD obligations.¹³ These supervisory authorities will be empowered to investigate alleged violations of companies' CSDD obligations (including in response to complaints submitted by individuals or legal persons), order companies to cease infringing activities, direct companies to take remedial actions, adopt interim measures to prevent immediate harm, and impose financial sanctions based on a company's turnover.¹⁴

- **Civil liability for non-compliance**

Each EU Member State must provide for companies to be liable for damages if they fail to comply with their obligations to prevent or mitigate potential HEIs, or bring to an end or minimise actual HEIs, and such failure leads to damage.¹⁵

- **Directors' Duties**

Directors of companies incorporated in the EU must consider, as part of their duty to act in the best interest of the company, the sustainability consequences of their decisions – including the human rights, climate change, and environmental consequences in the short, medium, and long term.¹⁶

- **Oversight of CSDD**

Directors of large¹⁷ EU-incorporated companies

- must take responsibility for putting in place and overseeing CSDD measures.¹⁸

Why should businesses in Asia care about the proposed Directive?

The proposed Directive is likely to have far-reaching implications for businesses across the globe – including in Asia. ASEAN is the EU's third-largest external trading partner, accounting for more than EUR 189 billion of trade in goods in 2020 – of which over EUR 120 billion were imports from ASEAN.¹⁹ Changes to business and human rights regulations at the EU level are therefore likely to have substantial repercussions for this market.

While commentators have been disappointed by the exclusion of small and medium sized enterprises (SMEs), from the proposed Directive,²⁰ the Directive nonetheless has the potential to have significant direct and indirect effects on companies in Asia.

Direct effects on Asian businesses

The Directive would impose obligations not only on companies incorporated in EU Member States, but will directly apply to all companies incorporated outside the EU that generate certain amounts of revenue in the EU. Lower turnover thresholds apply to companies in high-risk industries.

¹³ Directive, Article 17.

¹⁴ Directive, Article 18-20.

¹⁵ Directive, Article 22.

¹⁶ Directive, Article 25.

¹⁷ I.e., companies incorporated inside or outside of the EU with a net annual turnover in the EU of at least EUR 150 million.

¹⁸ Directive, Article 26.

¹⁹ European Commission, Association of South East Asian Nations (ASEAN). Available at:

<https://ec.europa.eu/trade/policy/countries-and-regions/regions/asean/>

²⁰ Contrary to the UNGPs – which require all businesses, regardless of size, to engage in HRDD based on the significance of their human rights impacts.

The Directive will directly apply to companies incorporated outside of the EU which generate a net annual turnover in the EU of:

- (a) EUR 150 million;²¹ or
- (b) more than EUR 40 million but less than EUR 150 million – if the company generates at least 50% of its net annual worldwide turnover in a high-risk industry. These are:
 - i. textiles, leather, leather and leather-related products (including footwear), and the wholesale trade of textiles, clothing, and footwear;
 - ii. agriculture, forestry, fisheries (including aquaculture), the manufacture of food products, and the wholesale trade of agricultural raw materials, live animals, wood, food, and beverages; and
 - iii. the extraction of mineral resources, the manufacture of basic metal products, other non-metallic mineral products and fabricated metal products (except machinery and equipment), and the wholesale trade of mineral resources, basic and intermediate mineral products.²²

The proposed Directive would therefore not just apply to the largest Asian exporters and service providers to the EU. It would also apply to mid-to-large-sized companies operating in high-risk industries such as textiles, agriculture, forestry, fisheries, and natural resources-extraction – which form the basis of many economies in Asia. Companies that could potentially be directly subject to the Directive include global brands such as Japan’s Toyota (2021 EU revenue of EUR 31.3 billion)²³ and Sony (2020 EU revenue of EUR 18.1 billion),²⁴ South Korea’s Samsung (2021 EU revenue of EUR 40.2 billion),²⁵ as well as Thailand’s CP Foods (2020 EU sales revenue of EUR 1.5 billion),²⁶ Thai Union (2021 EU revenue of EUR 1.2 billion),²⁷ and Indonesia’s Indofood (2020 global revenue excluding Asia, the Middle East, and Africa, of EUR 205 million),²⁸ as well as a range of smaller producers and exporters in high-risk sectors.

²¹ Directive, Article 2(2)(a).

²² Directive, Article 2(2)(b).

²³ Statista, Toyota’s revenue in FY 2021, by region. Available at: <https://www.statista.com/statistics/279652/revenue-of-toyota-by-region/>

²⁴ Sony, Supplemental Information for the Consolidated Financial Results for the Fourth Quarter Ended March 31, 2021.

Available at: https://www.sony.com/en/SonyInfo/IR/library/presen/er/pdf/20q4_supplement.pdf

²⁵ Samsung, Consolidated Financial Statements of Samsung Electronics Co., Ltd. and its Subsidiaries, 31 December 2021.

Available at: https://images.samsung.com/is/content/samsung/assets/global/ir/docs/2021_con_quarter04_all.pdf

²⁶ CP Foods, Annual Report 2020.

Available at: https://www.cpfworldwide.com/storage/annual_review/pdf_enpdf_enAnnual_Report_2020_Update_1617277319_1617781535.pdf

²⁷ Thai Union, Consolidated and separate financial statements, 31 December 2021.

Available at: <https://investor.thaiunion.com/misc/FS/20220223-tu-fs-fy2021-en.pdf>

²⁸ Indofood, Annual Report 2020. Available at: https://www.indofood.com/uploads/annual/ism_2020ar_web.pdf

Indirect effects on Asian businesses

Businesses in Asia that are not directly subject to the Directive are still likely to feel its effects. Companies that are subject to the Directive will be required to conduct CSDD on all parties in their value chain with whom they have an ‘established business relationship’ – anywhere in the world.²⁹

Thus, a company in Asia that is a direct or indirect supplier to a company that is subject to the Directive could be required to take part in CSDD procedures. This may be the case even if the supplier does not do any trade with the EU at all – or indeed, does not do any international trade.

Potential indirect effects of the proposed directive include:

Onboarding procedures and new contractual obligations for suppliers:

Asian-based suppliers that form part of the value chain of a company that is subject to the Directive might be required to undergo CSDD procedures during the supplier onboarding process. Purchasers may introduce new contractual provisions in purchase orders to require suppliers (and sub-suppliers) to comply with human rights codes of conduct and environmental standards.³⁰

Enhanced third-party audits and penalties for non-compliance

Suppliers may be required to participate in third-party audits and verification procedures to confirm compliance.³¹ As the Directive also provides for the possibility of civil liability for breaches of CSDD obligations, purchasers may also seek to pass on those risks to suppliers by including contractual indemnities or other business penalties such as a reduction in business volume, or the suspension or termination of business relationships³² in the event of non-compliance by suppliers with purchasers’ human rights and environmental policies.

Sustainable purchasing and procurement practices:

The proposed Directive may affect purchasing and procurement practices which could indirectly affect Asian-based suppliers. Companies that are subject to the EU may impose stricter requirements in the selection of their suppliers to facilitate conducting CSDD in their value chain – for example, by requiring suppliers to demonstrate that they have human rights and environmental policies and procedures in place, meet certain human and environmental certification standards, and have the infrastructure and capacity to participate in third party audits and independent verification. Companies that are unable to meet these requirements may find themselves less competitive in securing orders and tenders from business partners that trade with the EU.

²⁹ An ‘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 (Directive, Article 3(f)). This concept has raised concern among several commentators. It is not used in the UNGPs – which cover all business relationships, whether established or not. The confinement of CSDD obligations to established business relationships has the potential to narrow the scope of companies’ CSDD obligations by excluding business partners with whom a company may have short or one-off relationships. This can be a particular problem in the garment industry, where ‘fast fashion’ purchasing practices mean that orders may be fulfilled by temporary or one-off suppliers, sub-suppliers, or sub-sub-suppliers.

³⁰ The use of such contractual assurances is one means by which companies can demonstrate compliance with their CSDD obligations (see Directive, Articles 7(2)(b) and 8(3)(c)).

³¹ Directive, Articles 7(4), and 8(5). It should be noted however that the proposed Directive’s reliance on third-party audits and contractual assurances to demonstrate compliance has also been criticised by commentators, who consider that a greater emphasis should be placed on engagement with stakeholders from workers, civil society, and other interested groups to demonstrate compliance.

³² The Directive contemplates that the suspension or termination of business relationships with third parties is one way in which companies may address actual adverse HEIs that arise in the course of a business relationship. See Article 8(6).

New or expanded grievance mechanisms and access to remedy:

Suppliers in Asia could find themselves being required to make grievance and complaints channels accessible to their workers. These could include company-operated grievance mechanisms established by companies that are directly subject to the Directive, or grievance mechanisms operated through industry associations and bodies. Larger first-tier suppliers might also be required by their counterparties to establish their own operational grievance mechanisms for their employees.

Sustainability - linked trade finance and credit arrangements:

Financial services firms will also be required to conduct CSDD before providing credit, loans, or other financial services. This means that importers and exporters could face enhanced CSDD procedures, for example, when seeking trade finance or export credit arrangements from banks based in, or with operations in, the EU. Financial services³³ providers may also terminate credit, loans, or other financial services arrangements with third parties where actual adverse HEIs are identified – though the Directive provides that this is not required if it would cause substantial prejudice to the party receiving such financial services.³⁴ Alternatively, suppliers with a poor record of human and environmental rights compliance may face higher interest rates and fees when seeking financing, reflective of their increased risk profile.³⁵

What could the proposed directive mean for my business?

While the proposed Directive in its current form is not perfect, it nonetheless has the potential to transform the landscape of business and human rights in Asia. There are currently no jurisdictions in Asia that have established human rights due diligence or disclosure laws (including anti-modern slavery laws).

Companies in Asia that have until now not been subject to any mandatory CSDD or human rights disclosure obligations could soon therefore find themselves needing to establish CSDD mechanisms, produce CSDD disclosures, establish complaints channels, and develop remedial and corrective action plans.

It is also important to note that even businesses which are already familiar with reporting and due diligence requirements under anti-modern slavery laws may need to revisit their operations and procedures in light of the Directive. This is because the Directive covers a much broader range of human rights (including economic and social rights), labour rights, and environmental rights than most modern slavery laws – which are typically focused on forced labour, child labour, and human trafficking.

³³ Directive, Article 6(3).

³⁴ Directive, Article 8(7)

³⁵ This is already an emerging practice in many jurisdictions. See, e.g., the Loan Market Association, Asia Pacific Loan Market Association, and Loan Syndications and Trading Association Green Loan Principles. Available at: <https://www.lsta.org/content/green-loan-principles/>.

The Directive includes rights such as the prohibition on unlawful eviction or the taking of land for development, indigenous peoples' rights to traditional lands, territories, and resources, the right to equal treatment and non-discrimination in employment, and the right to enjoy just and favourable conditions of work including a fair wage, a decent living, safe and healthy working conditions, and reasonable limitation of working hours.³⁶

Businesses should therefore not assume that policies and processes that have been designed to identify and address 'modern slavery' will be fit for purpose to address the much more comprehensive range of rights covered under the Directive.³⁷

What should I do now to prepare?

While the proposed Directive is likely to undergo further negotiations and revisions before being enacted – and would provide for an initial two-year transition period – businesses in Asia would do well now to consider how, and in what ways they may be affected by the Directive. This includes:

- **Conducting a thorough assessment** to identify potential and actual adverse HEIs arising from their operations and value chains, having regard to the salience and significance of those impacts.
- **Reviewing existing human rights and environmental policies** to consider whether, and to what extent, they are compatible with the expectations and obligations imposed under the Directive, as well as the UNGPs.

- **Establishing procedures and mechanisms** to proactively monitor and identify actual and potential HEIs arising from their operations and value chain and to prevent, mitigate, and eliminate such risks where identified. Such processes should adopt a salience and risk-based approach to prioritising the management of risks. Where such mechanisms already exist, reviewing and updating those mechanisms to ensure they are compatible with the standards and expectations of the Directive and UNGPs
- **Conducting thorough due diligence** on their own suppliers and business partners to ensure that they have their own robust human rights and environmental policies and procedures in place, and to identify any actual or potential adverse HEIs arising from those business relationships. This is especially important for businesses that regularly rely on labour outsourcing and subcontracting arrangements.
- **Reviewing existing operational grievance mechanisms** to ensure that they are in line with the expectations of the Directive, UNGPs, and international guidance.³⁸

³⁵ Directive, Annex.

³⁶ It should be noted that unlike the UNGPs, the Directive does not cover the full range of human rights set out in the International Bill of Human Rights (the International Covenant on Civil and Political Rights, the International Covenant on Economic and Social Rights)

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³⁸ E.g., The Remedy Project and IOM [Operational Guidelines for Businesses on Remediation of Migrant-Worker Grievances](#), Customs Tariff, SC 1997 c.36, Chapter 98 and Canada-United States-Mexico Agreement Implementation Act, SC 2020, c. 1.

The proposed Directive should also be considered in light of the development of human rights-based sanctions and import ban regimes. In recent years, United States Customs and Border Protection has imposed import bans on suppliers in Asia whose products are alleged to be tainted by forced labour and has used ‘Withhold Release Orders’ to freeze shipments of such products already in the United States. Canada introduced a forced labour import ban mechanism in 2020,³⁹ while the Australian Senate passed a forced labour import-ban law in August 2021.⁴⁰

Despite the proposed Directive not including trade-based penalties or economic sanctions provisions, the European Commission has announced its intention to introduce a mechanism to prohibit the placing on the EU market of products made with forced labour or child labour to complement the proposed Directive.⁴¹ Establishing robust CSDD procedures and remediation mechanisms to provide redress for affected persons will therefore also provide businesses with a means of both proactively addressing trade and sanctions-related risks.

Contact us

For more information about this Briefing, and to find out how The Remedy Project can help support you or your business to prepare for the era of CSDD, contact us at: Archana@remedyproject.co

You can also reach us through our [website](#) or connect with us on [LinkedIn](#)

³⁹ Customs Tariff, SC 1997 c.36, Chapter 98 and Canada-United States-Mexico Agreement Implementation Act, SC 2020, c. 1.

⁴⁰ Customs Amendment (Banning Goods Produced by Forced Labour) Bill 2021. The bill has not however been taken up by the House of Representatives, meaning it is unlikely to pass into law. See: https://www.aph.gov.au/Parliamentary_Business/Bills_Legislation/Bills_Search_Results/Result?bld=s1307

⁴¹ European Commission (23 February 2022) Communication of from the Commission to the European Parliament, The Council, and The European Economic and Social Committee on Decent Work Worldwide for a Global Just Transition and a Sustainable Recovery. Available at:

<https://ec.europa.eu/social/BlobServlet?docId=25260&langId=en>. European Commission, State of the Union Address 2021.

Available at: https://ec.europa.eu/info/sites/default/files/soteu_2021_address_en_0.pdf; European Parliament, Legislative Train 02.2022.

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