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## The Corporate Sustainability Due Diligence Directive would ensure a level playing field and enhance necessary corporate sustainability

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### The Corporate Sustainability Due Diligence Directive at risk

In December 2023, following a lengthy Trilogue, a political agreement was reached regarding the Corporate Sustainability Due Diligence Directive (CSDDD); the first EU economy-wide mandatory due diligence legislative measure. The Directive aims to promote sustainable corporate conduct across global value chains, which include the full range of activities involved in the creation of a product or service. While the CSDDD is not a panacea, it is expected to foster a level playing field and improve corporate sustainability. However, a last-minute announcement from the internally divided German government to abstain from voting in the European Council has put the Directive's future at risk.

Despite earlier endorsement, on the 1<sup>st</sup> of February 2024, Germany suddenly [withdrew its support](#) for the CSDDD due to the opposition of the FDP, the liberal government coalition party. Lukas Köhler, FDP deputy head in German Parliament, [stated](#) that the FDP cannot support the Directive as its obligations would overburden companies. Subsequently, [other EU Member States, such as Italy](#), followed Germany's example and decided to abstain from voting, or to vote against approval. The Council vote which was initially planned on 9 February had to be postponed since the required qualified majority would not be reached. On 28 February, once again, due to lack of support, it was decided to postpone the vote on the approval of the Directive. In the meantime, the Belgian Presidency of the Council, [reportedly](#), proposed a new compromise text of the Directive hoping to convince Member States to vote in favour. The revised version would have included a downsized personal scope of application and softened provisions on civil liability. However, on 8 March, the

Council vote has again been postponed. While time is running out ahead of the European elections, the Directive has been set on the [agenda](#) of the Coreper I meeting on 13 March.

This blog post argues that the failure to approve the CSDDD by the Council under the guise of protecting companies is counterproductive and represents a missed opportunity in mitigating climate change. First, the post looks at the CSDDD from the perspective of European businesses. Then, it connects the urgent societal challenge of climate change to the EU Directive awaiting approval by the Council.

### **European companies embrace harmonisation**

Abstaining from voting, and, thus, *de facto* making approval impossible, is not in the interest of European companies. Indeed, the CSDDD would serve the companies' interests by seeking to harmonise due diligence legislation within the EU internal market. Pursuant to its dual legal basis (Art. 50 and 114 TFEU), the Directive aims to harmonise legislation to ensure a level playing field within the EU internal market and avoid distortions of competition. It is for this reason that European businesses urge the EU Member States to formally adopt the CSDDD. In a [joint statement](#), large German companies argue that putting the CSDDD at risk will create legal uncertainty. In their view, the Directive is the 'only chance' for an EU-wide level playing field with fair competitive conditions that will create legal certainty. Not only big companies embrace the CSDDD; the Italian Confederation of Craft Trades (CNA) representing small and medium-sized enterprises has, for example, [expressed](#) its support to the CSDDD as it will ensure a level playing field and avoid unfair competition with non-EU companies.

The fears of these companies regarding an unlevel playing field and legal uncertainty appear to be well-founded. Disparities between national due diligence legislation result in legal fragmentation which can lead to distortions of competition. Most notably, Germany and France have enacted legislation containing due diligence requirements. The legislative measures significantly differ in personal scope, material scope and regulatory approach. For instance, the [German act](#) applies to companies employing more than 1000 employees, whereas the [French act](#) only applies to companies employing more than 5000 employees. Moreover, under the French act climate change should be addressed in carrying out due diligence, while the German act does not cover climate change issues at all. Considering just these two examples of legislation, it becomes apparent that the risk of legal fragmentation should be taken seriously.

The Commission convincingly argues in the [proposal for the CSDDD](#) that these disparities between national legislation are likely to lead to distortions of competition within the internal market. Companies that are active in certain EU-jurisdictions with no or less stringent due diligence legislation will have a competitive advantage. Furthermore, legal

fragmentation creates a significant burden to companies as compliance with different national legislation requires diverging measures and policy per jurisdiction. Against this background, it should be noted that rejection of the CSDDD could even lead to further legal fragmentation. National legislative proposals, such as a [Dutch proposal](#), that were put on hold, awaiting the CSDDD, could be rehabilitated. Indeed, one could argue that not the CSDDD's requirements, but the lack of harmonisation will overburden European companies.

Alongside the harmonising effects of the CSDDD within the EU, the Directive's requirements align with international standards on due diligence. Since their adoption in 2011, the [UN Guiding Principles on Business and Human Rights](#) (UNGPs) and [OECD Guidelines for Multinational Enterprises](#) are internationally broadly recognised soft law documents that pursue corporate sustainability through encouraging due diligence regarding human rights and the environment. The approval of the CSDDD would strengthen these influential international standards, which have been [endorsed by the EU](#) since 2011. [According to the UN High Commissioner for Human Rights](#), the EU would show historic global leadership. Additionally, companies that already pursue to comply with these international due diligence standards will be rewarded for their efforts in carrying out business activities responsibly. Unsurprisingly, a large and wide-ranged group of European businesses [called for](#) an ambitious CSDDD aligning with the UNGPs and OECD Guidelines for Multinational Enterprises.

### **Corporate sustainability legislation for a green EU economy**

Building upon the existing international due diligence standards, the CSDDD, *inter alia*, seeks to advance the greening of the EU economy. Arising from the EU [sustainable corporate governance initiative](#), the CSDDD is a proposal for corporate sustainability legislation, crucial in steering towards a green and climate-neutral EU economy by 2050 as required by the [European Climate Law](#). Additional mitigating efforts are indeed necessary to address the urgent challenges posed by climate change. Last year, the International Panel on Climate Change (IPCC) [established](#) that human activities had already caused a global temperature rise of 1.1°C by 2020 in comparison to pre-industrial levels. Moreover, it revealed that current global mitigation efforts are insufficient to limit global warming to 1.5°C as envisioned by the [Paris Agreement](#). Similarly, the European Environmental Agency [has concluded](#) that current EU-efforts will not suffice to achieve the climate change mitigation goals codified by the European Climate Law. According to the IPCC, resilient climate policy will require 'large and sometimes disruptive changes in economic structures'.

Since the CSDDD is based on existing soft law, it does not seem to be that disruptive, yet it will target the right actors with substantive obligations. Addressing the private sector is

necessary as large companies are currently and historically have been the main contributors to climate change. The [2017 Carbon Majors Report](#) showed that just 100 companies are responsible to 71 per cent of all global greenhouse gas emissions since 1988. Regulation of sustainable corporate conduct has come a long way. Prior to the [European Green Deal](#), the EU predominantly aimed to enhance corporate sustainability through supporting and promoting voluntary corporate social responsibility (CSR). However, open-ended CSR initiatives and non-legally binding international due diligence standards leave a regulatory gap and do not suffice in effectively pursuing sustainable corporate conduct (see, e.g. [the study for the Commission on supply chain due diligence](#)).

The CSDDD partly seizes the opportunity to bridge this regulatory gap. The cautiously drafted Directive, as negotiated in the political agreement, contributes to the EU's climate change mitigation objectives rather half-heartedly and does not seem to fulfil the Directive's potential. In truth, the CSDDD's text has been watered down significantly. Both the Commission's proposal and the [European Parliament's draft report](#) were less cautiously drafted and would have been more effective in mitigating climate change. In this context, the political agreement's personal scope of application is fairly narrow. According to the political agreement, the Directive applies to EU companies with over 500 employees and a net worldwide turnover of at least EUR 150 million, and to non-EU companies with a net EU turnover of at least EUR 300 million. As a result, the revenue threshold for non-EU companies has, for example, been doubled compared to the Commission proposal. Additionally, the political agreement fails to designate any high-risk business sectors with lower employee base and revenue thresholds. Although the current text does not fulfil the Directive's potential, adoption would still be a crucial step into the right direction. The companies concerned are required to comply with two main substantive obligations.

Firstly, the due diligence obligation of Article 4 of the Directive requires companies to address adverse impacts of their business activities to specific human rights and environmental norms. Rather surprisingly, the political agreement fails to refer to any directly climate-related rights and norms. Noteworthy, the European Parliament was keen on directly addressing climate change through the due diligence obligation. Although not specified, the reason for not directly including adverse climate impacts could be that this due diligence obligation would, by some, be regarded as too far-reaching. However, as it is increasingly accepted that climate change harms the realisation of human rights and environmental norms (see, e.g. [UN General Assembly Resolution 76/300](#) and the [Dutch Supreme Court's decision](#) in the *Urgenda* case), adverse climate impacts can (possibly) be considered as adverse human rights or environmental impacts. This would mean that companies must either way address the adverse impacts of business activities to the climate.

Secondly, the other main obligation does directly refer to climate change. Article 15 lays down the obligation to draw up a climate transition plan. Reinforcing the reporting obligation of the [Corporate Sustainability Reporting Directive](#) (CSRD), the CSDDD would require large companies to adopt and put into effect a plan that is in line with the European Climate Law. Companies falling within the personal scope of the Directive would be obliged to reconsider their business strategy and implement measures, through a best-efforts approach, to play their part in reaching climate-neutrality by 2050.

### **The way forward**

It is to be hoped that the Council will eventually formally approve the proposed Directive. The CSDDD is not only about holding companies accountable, but also about fostering a level playing field and ensuring fair competition within the EU internal market. The support for the CSDDD from European businesses underscores its importance in creating legal certainty and eliminating distortions of competition that arise from disparities in national legislation. Furthermore, in light of the urgent need to address climate change and the transition to a sustainable economy, the Directive represents a crucial step forward. Efforts of the Belgian Presidency in the Council must be efficacious to regain earlier-existing support which was present at the time of reaching the political agreement in December 2023. By voting in favour of the CSDDD, EU Member States would, at last, prioritise the long-term interests of European companies, society and the planet.