

| January 2022

EU Mandatory Human Rights and Environmental Due Diligence

Briefing Note No. 1 | [Dr Rachel Widdis](#), Director, Europe

INTRODUCTION

With several countries including Germany and Norway pressing forward with their own mandatory human rights due diligence laws, companies are awaiting the EU's Directive on mandatory human rights and environmental due diligence as a regional and potentially global standard that can help avoid patchwork of regulatory requirements. In this briefing note, we provide the latest on the proposed EU Directive, the expected scope, key steps expected from companies, and the Directive's expected accountability and liability mechanisms.

OVERVIEW

The EU Commission Sustainable Corporate Governance (SCG) initiative, including human rights due diligence in supply chains, has again been delayed. The Commission has given no precise release date, although there are expectations it will be February/March 2022, a full year after the European Parliament adopted its [recommendations](#) on Corporate Due Diligence and Corporate Accountability. This timing would suggest an EU level framework would come into force in 2025/26. Expected as a Directive, it could lead a global standard for responsible business conduct.

SCOPE

Current discussions indicate it would apply to 'large' companies, possibly those with over 500 employees, as well as publicly listed small and medium enterprises (SMEs) and 'high-risk' SMEs (to be defined) established in EU Member States. To ensure a level-playing field, it would also include companies domiciled outside the EU for goods or services delivered in the EU market. The drive towards mandatory obligations to conduct human rights and environmental due diligence recognizes that frameworks which rely on voluntary implementation (UNGPs, OCED Guidelines etc.) have proven insufficient to widely or effectively change practices.

A study by the EU Commission found that only one in three companies in the EU were undertaking due diligence on human rights and environmental impacts. As repeated delays in bringing forward the EU SCG initiative show, it is challenging in multiple ways. It was originally to include both obligations of human rights due diligence on certain companies, and Directors' responsibilities for this process and longer-term sustainability goals. Now, it is unclear if there will be one or two separate legislative proposals.

ABOUT ARTICLE ONE

Article One is a specialized strategy and management consultancy with expertise in human rights, responsible innovation, and social impact. We partner with the world's leading companies to drive transformative change that places people at the center of business.

Which companies will come within scope, the ‘depth’ of due diligence obligations across value chains, and provisions for civil liability are under scrutiny. The development of the EU proposal comes against a background of publicly expressed support from [industry](#), [investors](#), [civil society](#), and polls indicating [EU citizens](#) want strong corporate accountability legislation. As more EU States develop due diligence style legislation ([Legislative Developments](#)), we anticipate challenges for companies until an EU level framework reduces fragmentation. For example, the Netherlands announced that it will not wait for the EU and will proceed with introducing broad due diligence legislation. Concurrently, there is a ‘hardening’ of corporate accountability via litigation particularly in the UK and the Netherlands.

KEY STEPS TO PREPARE FOR MANDATORY DUE DILIGENCE

Going forward, companies operating in Europe may expect obligations to prevent and address adverse impacts on human rights and the environment linked to their activities and business relationships. Companies can prepare by putting in place a process for assessing and monitoring actual and potential adverse impacts, integrating and acting on their findings, tracking responses, and communicating on actions taken. As set out in the UNGPs, due diligence is primarily preventative. It is risk-based, proportionate and context specific. To get ready to comply with future mandatory due diligence requirements, we recommend companies implement the following steps:

- Map their value chain and, with due regard for confidentiality, disclose relevant information;
- Require business relationships, including suppliers and subcontractors, to implement policies in line with the company’s due diligence strategy (through contractual provisions, the adoption of codes of conduct, or certified and independent audits to verify compliance);
- Conduct meaningful and safe engagement with stakeholders, including with communities, trade unions, representative associations, and human rights defenders throughout their due diligence process;
- Provide a grievance mechanism to act as both an early-warning and mediation system;
- Publish their due diligence policies, including indicating whether subsidiaries are included in the parent company’s disclosures;
- Communicate information to potentially affected stakeholders about the measures in place;
- Track the effectiveness of measures adopted;
- Adopt and indicate all proportionate and commensurate policies and measures with a view to ceasing, preventing or mitigating potential or actual adverse impacts;
- Where needed, to prioritize mitigation efforts consistent with the basis in the UNGPs.

Until an EU level framework is in place, provisions for due diligence and accountability will differ across countries in Europe. Given the trend towards mandatory due diligence across supply chains, being prepared may involve building capacity specific to the impact of business on human rights and the environment. Companies will be called on to situate responsibility within their organization, and to put in

place a roadmap for rolling out group-wide measures to map, track, and act on potential issues. While third-party certification may assist due diligence, it is not expected to alter companies' responsibilities.

EVOLVING STANDARDS

The standards which companies are to observe will be more specific than the UNGP level of at minimum 'internationally recognized human rights'. The European Parliament recommendations and recent due diligence legislation at national level refer to a range of international and regional conventions, including specific instruments, for example, concerning children and migrant workers. While international environmental standards are relatively less well developed, newer laws such as the German Supply Chain Act specifically refer to certain environmental conventions. Further, the UN recently passed a resolution recognizing access to a healthy and sustainable environment as a universal [right](#). In practice, there are challenges to translating standards regarding human rights and environment into corporate obligations, as is apparent in the current EU legislative process. For example, the European Parliament recommendations refer to climate change, but it remains to be seen if or how an EU framework may oblige companies to establish science-based targets to reduce GHG emissions or be accountable for them. In terms of 'large' companies coming within the scope of legislation, the high threshold of 5,000 employees in the French Duty of Vigilance Law is reducing with newer legislation. The German Act includes entities there with over 3,000 employees, reducing to 1,000 employees in 2024. The Dutch 'building blocks' for legislation includes companies with over 250 employees. At EU level it is still unclear, but indications are that 'large' companies would align with the proposed Corporate Sustainable Reporting Directive (CSRD) (2021/0104), with scope including publicly listed SMEs and high-risk SMEs.

ACCOUNTABILITY AND LIABILITY

It is expected that companies will be obliged to have a grievance mechanism in place, appoint a 'human rights officer', and publicly disclose reports on measures taken to meet their due diligence obligations. The question of accountability, via fines, administrative sanctions and potential civil liability is under discussion at EU level. The German Act includes administrative sanctions only, and the Dutch proposal also favors administrative accountability. Depending on the systems in individual countries, a national regulator or competent authority may impose sanctions, potentially including:

- Sanctions and administrative fines proportionate to the size of a company's turnover, as well as exclusion from public procurement, aid and support schemes, and seizure of commodities, should the company have failed to meet due diligence obligations and if remedial action is not taken within the specified time;
- Temporary suspension of activities or ban on operating in the market, should failure to comply with the due diligence directive lead to irreparable harm.

The European Parliament recommendations suggest that administrative fines should be comparable in magnitude to fines currently provided for in competition and data protection law. For example, the EU's

General Data Protection Regulation (GDPR), provides for fines of 2% of the company's worldwide annual revenue or 10 million euro, whichever is the higher amount. We anticipate States will set up a regulator to monitor and enforce compliance with due diligence legislation. Their remit may range from capacity building to investigative power. The call for legislation to provide for civil liability reflects existing barriers to remedy for people and communities affected by the impact of business on human rights and the environment. The European Parliament recommendations specify that Member States shall make provision whereby companies can be held liable in civil law and provide remediation for harm that they, or entities under their control, have caused or contributed to by acts or omissions. Notably, it provides a defence of due diligence, under which it would be for the company to prove that it took all due care in line with the legislation to avoid harm, or that harm would have occurred even if all due care had been taken. Criminal liability of the corporate entity for repeated infringements of legislation or based on its 'failure to prevent' severe harms has been raised in campaigns at national level. While the direction which the EU Commission will take is not yet known, both administrative sanctions and civil liability are possible, consistent with the European Parliament recommendations.

At Article One, we help companies develop and implement human rights due diligence systems and prepare for these new regulatory requirements. To learn more, please get in touch with Rachel at rachel@articleoneadvisors.com