AmCham EU
SPEAKING FOR AMERICAN BUSINESS IN EUROPE

Consultation response

Proposal for a Directive on corporate sustainability due diligence (CS3D)

AmCham EU speaks for American companies committed to Europe on trade, investment and competitiveness issues. It aims to ensure a growth-orientated business and investment climate in Europe. AmCham EU facilitates the resolution of transatlantic issues that impact business and plays a role in creating better understanding of EU and US positions on business matters. Aggregate US investment in Europe totalled more than €3 trillion in 2020, directly supports more than 4.8 million jobs in Europe, and generates billions of euros annually in income, trade and research and development.

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Executive summary

The American Chamber of Commerce to the EU (AmCham EU) appreciates the opportunity to provide feedback on the proposed Corporate Sustainability Due Diligence Directive (CS3D), and we strongly believe that Multi-stakeholder dialogue is the most efficient way to establish an operational framework that respects human rights and the environment across value chains.

The introduction of a common set of binding legal requirements on mandatory human rights and environmental due diligence for all sectors and companies irrespective of size furthers important objectives. Such requirements must, however, also serve to **combat growing internal market fragmentation** in this sphere, which is proving unworkable for companies. Legislation must **ensure that there is a level playing field** and that **requirements are the same for companies domiciled in or outside the EU**. The proposal needs to be improved to have an effective worldwide impact that supports the EU's global political and strategic ambitions.

It is important to ensure that the CS3D requirements are proportionate, risk-based and workable, and that they don't create operational barriers to international tradefor both EU firms with international businesses and non-EU firms with EU businesses.

Consistency with international frameworks and definitions

As is appropriate, the proposed CS3D is based on international standards such as the UN Guiding Principles on Business and Human Rights (UNGPs) and the Organisation for Economic Co-operation and Development (OECD) Guidelines for Multi-National Enterprises (MNE) and the International Labour Organization (ILO) Declaration on Fundamental Principles and Rights at Work. Since the adoption of these international standards, numerous businesses across the world have taken steps to voluntarily align with the framework outlined therein and established due diligence schemes that consider the specific nature of each sector to provide assurance to customers and stakeholders. Thus, the EU proposal's **coherence with globally established measures** would allow European and third-country companies to implement efficient and harmonised due diligence mechanisms in their value chains.

Considering what is already included in the international standards and the very nature of due diligence practices, there is a **need for a 'risk-based', proportionate and context-specific approach;** it is important to avoid significant deviation from these international standards. Likewise, some definitions included in the proposed text require a closer look.

Due diligence duty

The proposal's intention to promote human rights and the safety of workers in global value chains, as well as certain environmental impacts, is admirable. However, it is important not to confuse the roles of companies and states. In the field of human rights, the division between the state's responsibility to protect and the business's responsibility to respect must be embedded in any legislative initiative. In this vein, due diligence duty - which should follow a risk-based approach - and liability - which should be limited to direct established business relationships - should be decoupled.

- **Due diligence duty should be consistent with existing international frameworks** such as UNGPs, ILO Declaration on Fundamental Principles and Rights at Work and the OECD MNE Guidance. These have guided the implementation of existing robust due diligence schemes, more specifically the model the OECD Due Diligence Guidance for Responsible Business Conduct guidelines on how to implement a risk-based due diligence approach; Chapter 2 of the OECD Guidance on how to 'identify and assess actual and potential adverse impacts associated with the enterprise's operations, products or services' clearly distinguishes between two consecutive steps: risk identification and in-depth assessments of prioritised supply chains.

- Due diligence legislation should not impose specific sustainability requirements on companies or liability on individual directors. Companies should be able to choose how (eg specific targets) they meet their sustainability requirements as they strongly vary between companies, sectors and issues. Overly onerous and imprecise requirements on individual directors should be avoided, as they could discourage highly qualified individuals from taking up directorships of European companies.

Established business relationships

The **definition of 'established business relationships**,' which also determines the scope of due diligence, needs to be better defined but **should not be expanded** to take on additional scope beyond what is already understood within existing international frameworks. In frameworks including UNGPs, OECD MNE Guidelines, 'business relationship' is described as relations of the enterprise with business partners, suppliers, contractors and entities directly linked to its business operations, products or services. **Civil liability should be limited to those**

relationships in which companies have the legal means of enforcement and recommend that the legislation cover **only direct contractual business relationships within the supply chain**. This would be most likely via a contractual relationship, with links to causing or contributing to an impact and an associated level of responsibility for correction and remedy. While the Explanatory Memorandum clarifies that civil liability concerns only established business relationships in which a company expects to have a lasting relationship, this is not sufficient to provide companies with legal certainty around their liability in case of violations. In practice, suppliers and subcontractors positioned at the end of the value chain are difficult to identify; the company has no leverage, influence or control over them. **Companies should not be held liable for entities they may not even know exist, much less influence or control.** Thus, the inclusion of suppliers and subcontractors that are indirectly linked to the undertaking or placed at the very end of its value chain is problematic and potentially impractical. The same would be true at the other end of the value chain with respect to customer use and disposal of products. Conducting due diligence on end users is a practical impossibility, regardless of the seller's efforts. For those reasons, **the definition of established business relationships and other relevant provisions should impose a legal obligation to conduct due diligence on upstream relationships only**. Moreover, an 'established relationship' is described as one that is 'lasting'. This has the potential to incentivise suppliers to distance themselves from long-lasting supplier relationships and seek out short-term commitments, which goes counter to the intention of the requirements.

Any civil liability should be limited to severe human rights and environmental harms[1] caused by the company's own activities or activities of controlled companies, excluding third parties such as suppliers, which could have been prevented had the company fully complied with the requirement to conduct human rights and environmental due diligence. What constitutes a 'severe human right and environmental harm' must be defined in interpretative guidance following constructive dialogue amongst all relevant stakeholders, taking account of already existing legal instruments or standards. The limitation of the scope of civil liability to controlled companies is aligned with the approach proposed by the European Parliament in its March 2021 Resolution on Corporate Due Diligence and Corporate Accountability.[2] Nonetheless, the European Parliament's **definition of 'control'** leaves too much room for interpretation and does not provide sufficient legal certainty for companies.

The definition of 'control' should imply the **possibility of an undertaking to exercise decisive influence on another undertaking by ownership of over 50% of the voting rights**, which confer decisive influence on the composition, voting or decisions of the decision-making bodies of an undertaking. Such a definition would provide companies with legal certainty and ensure that their legal liability covers situations where they can effectively exert control over other parties to prevent or mitigate adverse impacts on human rights or the environment. **The OECD Due Diligence for Responsible Minerals Supply Chains** (3rd. Ed, 2016) is an effective international framework for identifying the due diligence responsibilities of companies with suppliers with whom a **direct relationship** exists (pp39,40) and highlighting the role of collaboration and associations to build capacity, due diligence and standards further upstream in the supply chain (pp42, 45).

[1] Definition as per UNGP glossary on https://www.ungpreporting.org/glossary/severe-human-rights-impact/: A negative human rights impact that is severe by virtue of one or more of the following characteristics: its scale, scope or irremediability. Scale means the gravity of the impact on the human right(s). Scope means the number of individuals that are or could be affected. Irremediability means the ease or otherwise with which those impacted could be restored to their prior enjoyment of the right(s).

[2] Art 3(9)"'control' means the possibility for an undertaking to exercise decisive influence on another undertaking, in particular by ownership or the right to use all or part of the assets of the latter, or by rights or contracts or any other means, having regard to all factual considerations, which confer decisive influence on the composition, voting or decisions of the decision making bodies of an undertaking."

Similarly, the OECD-FAO Guidance for Responsible Agricultural Supply Chains delineates a scope for due diligence obligations, depending on the type of enterprise and position in the value chain (p36), and recommends that when enterprises have large numbers of suppliers, they are encouraged to identify areas where the risk of adverse impacts is most significant and, based on this risk assessment, prioritise suppliers for due diligence (p22).

The definition of '**value chain'** is too vague and not frequently applied in the field of human rights and environmental due diligence. Moreover, 'value chain' could be interpreted as including the end use of products, which is extremely difficult to control and detracts from the identification and mitigation of salient risks in supply chains.

Environmental due diligence

While there is a certain level of clarity regarding companies' duties to carry out due diligence against human rights impacts in the proposal, the **scope of environmental due diligence** remains vague. Additionally, there needs to be due consideration for potential risks of duplication or contradiction with existing and forthcoming environmental and climate-related EU legislation and international standards, including clarification of which environmental standards companies should be held to. In short, the CS3D should not be a mechanism to regulate greenhouse gas emissions, which is being done elsewhere. A clear and univocal definition of environmental due diligence should be introduced to determine its scope before obligations are imposed on business.

Coherence between European Legislative Frameworks

The European Commission has sought to **bring alignment and coherence** between the various existing and forthcoming legislative frameworks broadly related to sustainability or to due diligence limited to certain sectors, a much-appreciated consideration. Nevertheless, companies need more clarity and guidance at this stage. To ensure full policy coherence, more clarification is needed on the **relationship between the proposed CS3D and the corporate sustainability reporting directive** for which sustainability reporting standards are being elaborated on by the European Financial Advisory Group, as well as **other sectoral laws that contain due diligence requirements** (eg batteries, deforestation or minerals regulations).

Industry schemes and sectoral guidelines

Importantly, the proposal acknowledges relevant industry schemes such as the Responsible Business Alliance (RBA) which, as mentioned above, numerous companies have adhered to and put in place in past years, including supply chain risk assessment, onsite externally verified audit, specific social and environmental monitoring and reporting programmes, self-assessment questionnaires, capability-building, engagement and dialogue tools and quarterly business reviews. The importance of similar schemes and programmes has demonstrated to be effective in identifying and preventing human rights violations in supply chains while giving to companies the necessary level of flexibility to comply with requirements based on their sector and operations. **A mechanism should be built into the CS3D legal framework to recognise existing and future industry schemes, as is the case with the Conflict Minerals Regulation**. These schemes should serve to give companies a minimum level of flexibility to comply with the requirements. Membership of such schemes should help companies to comply with the rules and complement their due diligence programmes. They should not be a smokescreen for companies to fail to conduct due diligence in their value chains.

Collaborative partnerships such as the highly successful **European Partnership for Responsible Minerals (EPRM) should also be encouraged** to help deliver on the legislation's goals. The CS3D should focus on engagement with affected stakeholders, the complaints mechanisms and ensuring remedy where harm has occurred. These would better align with international frameworks.

There is an evident need for companies to have **robust and clear guidance**. This should be **supplemented by sectoral guidance** that assesses an industry's due diligence approach, sometimes built up over several decades, and explains to what extent it needs to be adapted for the new requirements, while at the same time encouraging companies to go beyond compliance requirements.

The nature of global supply chains operating across a range of operational, trading, market and regulatory imperatives often require regular risk mitigation, in some cases when an issue has already arisen or when the company, despite due diligence practices, cannot identify and address a risk further upstream or downstream at the speed required. The EU legal framework should be **risk-based** and **recognise existing effective harmonised industry schemes** (see Annex with examples of successful industry schemes).

Civil Liability

While there is a need for effective enforcement of the proposed regime, there are also serious reservations about the far-reaching proposals for civil liability.

These proposals are unprecedented and would lead to **significant difficulties and uncertainties for businesses**. Insofar as they apply beyond companies' own operations to the 'value chain', they would effectively upend the established principles of tort law by making companies liable for damage not caused by their own actions, but rather by the actions of others. In this context, it would be difficult to meaningfully apply the normal principles of causation, which play a key role in delimiting the scope of civil liability. There is a real risk that companies would face excessive and disproportionate consequences.

The proposals could also have the perverse effect of shifting liability away from the actual perpetrators of the damages, should those who have suffered damage elect to simply sue the companies subject to the Directive in Europe, thereby diminishing the deterrent effect of possible civil liability.

Similar difficulties also arise with the proposal that companies should pay compensation as part of their general obligations to end the adverse impacts identified through their due diligence. Instead, an enforcement system based solely on the administrative model of the European supervisory authorities should be followed. Indeed, one of the main criticisms made by the Regulatory Scrutiny Board was lack of consideration of a stand-alone administrative supervision option. Under the proposed Directive, the supervisory authorities are to have significant investigative and enforcement powers, including the ability to investigate substantiated complaints and impose substantial sanctions. They would therefore be well-placed to ensure effective enforcement – a preferred model.

Other points for consideration

Potential adverse impacts

The last resort solutions identified in article 6 of the proposal for potential adverse impacts – in particular, the requirement to terminate the business relationship with respect to the activities concerned if the potential adverse impact is severe – does not align with the spirit of continuous improvement and helping 'all the boats rise with the tide'. Furthermore, especially in the case where the company may have limited leverage with the partner, this may lead to undue termination of the contract, as it may be seen as a simpler course of action. Also, suspending or terminating contracts based on potential impacts, without due verification of the nature and presence of those impacts, may have severe, unfair consequences on smaller suppliers. The potential for

companies to resort to terminating supplier relationships (due to limited leverage, potential adverse impact or short-term nature of their contract) also goes counter to the requirement for 'Companies whose business partner is an SME, are required to support them in fulfilling the due diligence requirements, in case such requirements would jeopardize the viability of the SME's.

Compensation for damages

The proposal's language is overly broad and does not adequately define who has the standing to assert a claim, what will be required to make a claim and how and who will prosecute.

Stakeholder engagement

The obligation around 'Affected Stakeholders' and 'Stakeholder Input' requires further definition (as in 'The prevention action plan shall be developed in consultation with affected stakeholders', 'Where relevant, the corrective action plan shall be developed in consultation with stakeholders' and 'Member States shall ensure that directors of companies...are responsible for putting in place and overseeing the due diligence actions...with due consideration for relevant input from stakeholders and civil society organisations').

Complaint mechanisms: 'legitimate concerns'

Article 9 requires companies to allow affected persons, trade unions and civil society organisations to submit complaints where they have 'legitimate concerns' relating to actual or potential adverse impacts. Furthermore, par. 3 also envisages the possibility for companies to establish procedures for complaints that they deem to be 'unfounded', yet it remains unclear as to what would constitute a 'legitimate concern'.

Responsible disengagement

The proposed Directive seems to recognise that temporary suspension of a relationship may be an appropriate use of leverage and that termination may be necessary where impacts are severe and mitigation efforts are not successful. However, the Directive should explicitly recognise that there may be additional human rights consequences associated with termination and should more clearly allow for 'responsible disengagement' strategies and considerations, particularly where the company lacks leverage in line with the UNGPs.

Assessment of liability

The proposed Directive contains a limited safe harbour from liability – if the company took certain steps, and it was reasonable to expect those steps would be adequate – for adverse impacts caused by an indirect partner with whom it had an established business relationship. While the Commission's effort to provide a safe harbour from liability, even if limited, is appreciated, it appears to set forth a subjective standard of reasonableness that may be difficult to demonstrate in practice.

Annexes

Human rights and environmental adverse impacts are defined by reference to an Annex that lists several international treaties, including the Convention on International Trade in Endangered Species of Wild Fauna and Flora, the Minamata Convention, the Stockholm Convention on Persistent Organic Pollutants and also the Basel Convention. With respect to environmental adverse impacts, the proposed Directive provides little clarity on how a company would identify or address an adverse impact associated with an international treaty when these treaties have not been drafted to apply to private corporations. Similarly, it is not clear how a company would demonstrate that its efforts were sufficient to qualify for protection from civil liability for any alleged failure by

an indirect partner to comply with the provisions set forth in a listed treaty. Further guidance specific to companies is needed.

Companies should be given safe harbour for antitrust concerns and other legal obligations

Articles 7(2)(e) and 8(3)(f) direct companies to, 'in compliance with Union law including competition law, collaborate with other entities, including, where relevant, to increase the company's ability to bring the adverse impact to an end'. Article 4(2) requires Member States to ensure companies are entitled to share information 'in compliance with applicable competition law'. However, these provisions require companies to anticipate the line that competition authorities will eventually draw between lawful and unlawful collaboration and to do so without any antitrust exemption. To address this, the cooperation provisions should be eliminated or an express antitrust exemption in an EU regulation should be included, as well as other applicable laws or contractual obligations that comply with the CS3D may require companies to violate (*eg* privacy, contractual confidentiality).

Consolidated reporting

Article 11 on reporting should provide the possibility for companies in third countries to refer to consolidated global reporting at group level. As companies determine fiscal years in different ways, the reporting obligation should allow for companies to annually report on due diligence within six months from the end of their fiscal year. This would ensure that the due diligence report would adequately cover the company's last accounting period.

Extraterritoriality – Scope of application and international coordination

While the proposed annex is based on international standards, we note that not all the countries around the world have signed, ratified and/or apply those conventions in full. As such, the extensive requirements in the proposal extend beyond other extra-EU jurisdictions. This might negatively impact EU companies' competitiveness and introduce substantial additional obligations for non-EU companies.

As the CS3D is set to **indirectly impose European standards on third-country businesses** (that might not be required by their national legislation to implement such norms), the **EU must provide absolute clarity about the obligations and responsibilities of such companies** in order for them to conduct business in an efficient manner and to continue to fruitfully engage with their European business partners. With regard to the financial sector, the proposed scope is likely to cover not only large international EU financial institutions at consolidated level, but also non-EU financial institutions with cross-border business and/or branches in the EU. This would require both EU and non-EU financial institutions with an EU presence to comply with the EU CS3D requirements throughout their global value chain. These third-country businesses are likely already subject to different requirements in other jurisdictions around the world. As it stands, the proposal would cover transactions with no connection to the EU.. This would include, for example, loans from a non-EU bank to a non-EU company selling goods or services to a non-EU customer. Such unprecedented extraterritorial application would be difficult to enforce.

To address this issue while maintaining a fair business environment for financial institutions headquartered in the EU and for those headquartered outside the EU, we propose that the scope should be limited to:

i) EU financial entities meeting the turnover and employee threshold at the highest level of EU consolidation; and

ii) EU branches of third-country banks meeting the turnover and employee threshold.

In addition, in regard to regulated financial undertakings' clients, the due diligence value chain should be limited to clients receiving loan, credit, financing, insurance or reinsurance services. As due diligence policies are often set at group level, financial institutions should also be able to defer to group policies when appropriate and in line with international standards and the objectives of the proposal.

As the new rules will ultimately have an impact on *any* foreign company involved in the value chain of European entities, we urge the co-legislators to **clearly define what is expected from non-EU companies** and to **provide guidance on how they can make sure that they are compliant without overburdening entities that are located in jurisdictions outside the EU**.

Conclusion

We once again appreciate the intent of the current proposal and the opportunity to provide feedback to be considered during the upcoming legislative negotiations. AmCham EU remains open to a constructive dialogue with all stakeholders to achieve a law that would successfully improve human rights and environmental aspects around the world while not overburdening companies, allowing them to conduct business in a fair way and giving national authorities the ability to enforce the rules accordingly.

ANNEX I – EXAMPLES OF SUCCESSFUL INDUSTRY SCHEMES

Automotive: Drive Sustainability (https://www.drivesustainability.org/drive-sustainability-strategy/)

Responsible Supply Chain Initiative RSCI (https://www.vda.de/vda/de/presse/Pressemeldungen/211028_VDA-gr-ndet-gemeinsam-mit-Herstellern-und-Zulieferern-den-Verein-Responsible-Supply-Chain-Initiative-RSCI-eV)

Textile: Better Work (https://betterwork.org/)

Sustainable Apparel Coalition (https://apparelcoalition.org/

Fair Labour Association (https://www.fairlabor.org/)

NOTE – RBA and EPRM ARE NOT TECHNOLOGY-SECTOR-SPECIFIC