Joint position paper

on the Proposal for a Directive on Corporate Sustainability Due Diligence

29 June 2022

Further to the position papers and declaration statements of their respective European associations[1], this document constitutes the Luxembourg Chamber of Commerce's and FEDIL's additional contribution to the proposal for a Directive of the European parliament and of the Council on Corporate Sustainability Due Diligence and amending Directive (EU) 2019/1937 (hereafter referred to as the "Proposal" or the "Directive").

I. Introduction

On 23 February 2022, the European Commission (hereafter the "Commission") published its Proposal of a Corporate Sustainability Due Diligence. The Proposal imposes upon in-scope EU and non-EU companies far-reaching obligations to set up and implement due diligence policies to identify, prevent or mitigate, and ultimately end, adverse impacts of their activities on human rights and the environment. The Proposal also introduces a specific obligation relating to climate change as well as a revised duty of care for directors regarding sustainability matters, along with a personal liability regime for directors of in-scope EU companies, actionable by stakeholders (as defined under the Directive).

The Chamber of Commerce of Luxembourg and FEDIL - The voice of Luxembourg's Industry, together with their members, understand the important role of due diligence in ensuring sustainability and respect of human rights and environment in business. We therefore welcome the initiative of the Commission to legislate at EU level for the purpose of establishing a harmonised legal framework.

However, the Proposal raises significant concerns, especially under the current conjuncture. Luxembourg industry and businesses managed to remain active during the years of the Covid pandemic, though not without struggles and slowdowns, where demand was low and so were profits. On top of that, the increasingly rising price of energy further aggravated the situation across various sectors of the economy. As if that was not challenging enough, the vile aggression of Russia against Ukraine and its consequences on the supply of energy, food and other materials weakened the economy more and more. In such a tense and unpredictable context, it the commendable legislative initiatives the EU has tabled under its Fit-for-55 package, and which businesses support, should also be considered as they are certainly posing harsh and expensive challenges to them. All these factors should be considered together. In light of this, it is clear that production as well as supply and logistics, have become fragile and costly and we therefore envisage that the implementation of the Directive, should it be adopted as proposed, would cause (or contribute to cause) the following consequences:

[1] FEDIL is member of BusinessEurope; the Luxembourg Chamber of Commerce is member of Eurochambres.

- difficulties to find raw materials, especially those mostly or exclusively located in 3rd countries, and to have access to energy sources, hence disruption of production and interruptions of supply chain which could ultimately result in shortages of related products and continuing price inflation;

- inconsistent application between and within EU Member States (hereafter "MS") and absence of sufficient level playing field between EU companies and with regard to non-EU companies, due to unclarity and inconsistency of many key provisions and unjustified discrepancies between rules applicable to EU and non-EU companies;

- additional administrative, compliance and staff related costs for companies, due to the very broad span of obligations and the complexity of the rules proposed as well as due to the absence of uniform standards and support schemes;

- real negative impact on companies' competitiveness, considering that out-of-scope non-EU companies, including competitors, will be significantly less affected - if not at all - by the Directive and may very likely benefit from the probable disengagement of EU companies from certain "problematic" non-EU jurisdictions, where violations of human rights and environment protection standards are continuing;

- high compliance costs and negative impact on companies' competitiveness are expected to have important social costs, such as unemployment in the EU; and

- finally, it cannot be completely excluded that in-scope companies decide to relocate their business outside of the EU and stop providing goods and services in the EU. That would be merely the result of non-availability or lack of raw materials and energy sources within the EU, and of an effort to avoid the significant costs that implementation of the Directive's unfeasible due diligence obligations may entail, especially regarding certain "problematic" non-EU jurisdictions.

We therefore consider essential that the ongoing legislative procedure should aim at:

- **avoiding additional fragmentation of internal market rules;**
- **ensuring uniform rules in all MS and adequate standardisation tailored to the specific sectors as well as consistency with existing frameworks**;
- **imposing proportionate, workable and enforceable rules on companies to effectively contribute to sustainable business conduct;**
- **mitigating any elevated risks associated with the implementation of the Proposal, such as price inflation, serious disruptions in certain supply chains and resulting critical shortages**.

In addition to the current legislative action at EU level, we invite the EU Institutions and the MS to continue and increase their efforts at global level as well, in order to successfully associate all relevant actors, both European and non-European, in that same endeavour.

The **Chamber of Commerce of Luxembourg** and **FEDIL - The voice of Luxembourg's Industry** have drafted this joint position paper which contains an executive summary of our key messages on the Proposal (section II.) and

a legal assessment of the main provisions of the text which have, or are likely to have, a significant impact for our members and their organisations, together with our key messages elaborated in detail (section III.).

II. Executive summary of key messages

Our key messages on the Proposal can be summarised as follows:

➢ **Introducing proportionate, workable, and more targeted rules for companies**

In practice, **it is very challenging, if not impossible,** for companies to control their whole value chain i.e., in addition to their own operations and the operations of their controlled subsidiaries, also the operations of entities with whom companies have an established (direct or indirect) business relationship. The proposed obligations are therefore **not reasonable nor workable** and companies should not be held responsible for events that are out of their control. Considering the far-reaching obligations (and associated liability) imposed upon companies, it should be expected that their operations will be impacted, leading to serious **impairment of their competitiveness**. For example, EU companies will have to withdraw from third-country "problematic" jurisdictions where it is already proven impossible - for various political and social reasons - to impose EU protection standards. Due diligence obligations should thus be **feasible and workable** and should only cover **the first-tier direct supplier(s) of in-scope companies**.

The Proposal makes no distinction between operations in the EU and operations outside of the EU, although in the EU territory there is already a very high standard regarding human rights and environment protection. Hence, it is not proportionate to impose on companies the same obligations in both their intra-EU operations and to extra-EU operations. The Directive should **differentiate the obligations within the EU and outside the EU**. In the same vein, **a more targeted due diligence regime** should be introduced, based on the most relevant adverse impacts, in respect of certain products and not any activity of the in-scope companies without any further distinction whatsoever as regards the actual risks for human rights and the environment involved.

In addition to the above, the introduction of a prioritisation system of suppliers based on country or industry-specific risks should be envisaged. Such a prioritisation system could be either factored-in the material scope of the Directive or provided for thereunder as an implementation measure for companies. The exclusion of small and medium-sized enterprises (hereafter "**SMEs**") is welcome. However, they will be indirectly affected as suppliers in the supply chain and will face challenges and contractual constraints. This will imply costs of implementation and unnecessary bureaucracy and burdens for SMEs, which should be avoided or, at least, mitigated with appropriate accompanying measures.

Moreover, competitiveness of EU companies active in third-country markets needs to be preserved. Otherwise, it is expected that non-EU competitor companies, which are not subject to such stringent rules, will probably take over those market shares, with negative consequences on employment as well as on prices and availability of products.

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➢ Ensuring an adequate level playing field and avoiding further fragmentation of EU internal market rules

(A) The Proposal creates an imbalanced situation as regards non-EU companies and does not to deliver the requisite **level playing field**. The turnover thresholds for non-EU companies in scope are much higher than for EU companies, considering that only their net turnover "generated" within the EU is to be accounted for. This implies that EU companies ultimately falling within the scope of the Directive will be smaller in size than in-scope non-EU companies. The turnover criteria should be the same **for both EU and non-EU companies** i.e., the **reference turnover should be that generated within the EU**.

(B) The Proposal leaves too much discretion to MS to legislate when transposing the Directive into national law. Such an important leeway left for MS may lead to further fragmentation of rules within the EU internal market. The Directive should **ensure full harmonisation of key provisions to deliver an adequate level playing field among MS** and **to ensure uniform rules and standardisation within the single market**. At least key provisions, especially those imposing obligations and requirements related to due diligence plans, reporting and information sharing obligations and liability, should be fully harmonised and coherent.

(C) On the face of it, the due diligence obligations established are set at company level and not at group level. Whilst we understand the reasons for this choice, the challenges for groups of companies *de facto* exposed to different national rules within the single market must be addressed. Groups of companies should have the flexibility to organise their due diligence plans according to their business model, thereby avoiding fragmentation of approaches and enhancing the effectiveness of due diligence strategies and actions within groups.

➢ Important definitions should be revised and clarified

In addition to the notion of "value chains", the following definitions should be revisited, i.e.:

(A) The terms "adverse environmental impact" and "adverse human rights impact" should be more precisely defined in order to allow for clearly defined obligations for in-scope companies and grant predictability to all stakeholders.

(B) The definitions of "**business relationship**" and "**established business relationship**" are very broad and unclear and do not cover certain "grey areas" of the supply chain. These concepts **need to be clearly defined and should be -in any case- limited to direct suppliers only**.

(C) The definition of "**stakeholders**" is extremely broad, considering that the obligations imposed upon companies concerning "stakeholders" are many and significant. This definition **should be narrowed down.** For example, "stakeholders" could be defined as those having specific attributes peculiar to them or by reason of circumstances that differentiate them from all other persons and having a specific and actual (or soon to occur) injury that is causally connected to the conduct concerned.

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(D) "**Appropriate measures**": the Proposal does not provide sufficient guidance to companies as to what is "reasonable" or not. Considering that the company's "influence" is to be taken into account when assessing **whether a measure is "appropriate" or not**, it still remains unclear which measures allow companies to comply with their due diligence obligations. **Companies need legal certainty as to whether the measures the have taken allow them to be compliant or not.**

➢ **Need for legal certainty, effectiveness and enforceability of due diligence obligations and the importance of standardisation**

The vague nature of the due diligence obligations and the absence of concrete criteria measuring companies' sustainability render the Directive theoretical in scope and do not provide companies with the necessary certainty as to whether they are compliant or not. The measures to be taken and the actions to be undertaken by in-scope companies clearly overlooked important practical issues affecting the effectiveness and enforceability of the Proposal's obligations.

The provisions on due diligence obligations need to be redrafted in a practice-oriented way to further provide companies with practical guidance as to how to carry out their due diligence exercise and prove their compliance.

In addition to Commission's guidelines, companies should be allowed to have recourse to standardisation schemes, such as unified labelling or certification systems, based on common standards and delivered by certified bodies. Moreover, standardisation should be tailored to the different sectors of activities. To this end, standards should be elaborated following consultation with business operators.

➢ **Model contractual clauses should be developed together with business, including SMEs**

They should be **available as soon as possible** to leave time to companies to implement them.

In this respect, it should be also considered that it is not always possible or feasible to negotiate their insertion into existing contracts with business partners or impose them upon more powerful third-country partners, and therefore their value might be limited in practice. As a consequence, the co-legislators need to take this into account and provide for more practice-oriented solutions that could in fact alleviate companies' burden.

➢ **Guidelines to companies and precise accompanying measures are needed**

The accompanying measures to support the Directive's implementation by companies are **neither sufficient nor appropriate**. The Directive, if adopted as proposed, might not facilitate in any way the introduction of these measures. **Common EU rules** should be introduced to **provide precise accompanying measures**. Moreover, **specific accompanying measures should also be introduced taking into account sectoral standards and needs**. Lastly, the **Commission should have a prominent and centralised role** in granting companies the needed information and support.

In order to provide support to companies or to MS authorities on how companies should fulfil their due diligence obligations, the Commission should issue additional and appropriate guidelines covering the activities concerned.

➢ **Obligations on climate change should not be included in the Directive**

The provision on climate change, if adopted as proposed, would only **create inconsistencies with already existing legislation**, while **adding further obligations** that are not related to the main purpose of the Proposal, which concerns due diligence and not climate change. Furthermore, this provision leaves **too much room for MS to interfere with well-established and functioning corporate governance models** and will **fragmentate even further the rules adopted within the EU**. This provision should be **deleted**, so that this issue can be properly dealt with by the other legislative instruments dedicated to it. In the alternative, this provision should be either **deleted** or - alternatively - **revised to provide precise rules and enforceable obligations, and not generic and inconsistent requirements further burdening EU companies without having any real added value.**

➢ **Sanctions and enforcement are not proportionate and lack guarantees**

(A) The proposed provisions on public enforcement are too intrusive, disproportionate and not appropriately counter-balanced with due process and appeal rights. They should be **revised as to ensure the proportionality and due process safeguards**.

(B) The concept of "public support" is **vague**, it could therefore lead to **legal uncertainty and to fragmentation of rules** within the single market. Moreover, this provision could violate fundamental principles of law insofar as it might lead to double punishment for the same facts, it does not contain any time limitation, it does not refer to the severity or nature of the breach. This provision should thus be **redefined** considering the above considerations or **deleted**.

(C) Public enforcement powers should be harmonised across MS to avoid fragmentation of rules and to ensure a level playing field within the EU. The Directive should therefore provide for more detailed rules regarding the set-up of supervisory authorities and their powers.

(D) Furthermore, it is necessary that the Directive ensure coordination among the different MS supervisory authorities, especially in the case where more than one companies from the same group are established in different MS. To this end, the Directive could provide for the establishment of a central authority overseeing its implementation across MS.

(E) Lastly, the competence granted to national supervisory authorities concerning substantiated concerns appear unlimited as they refer to any breach of the Directive's obligations. In addition, any stakeholder could bring a case before a supervisory authority. Only directly affected parties or entities with legitimate interest should have the right to file substantiated complaints, which should only refer to breaches of companies' due diligence obligations.

➢ **The proposed civil liability regime is in principle inadequate and needs considerable redrafting in line with EU civil law principles**

The civil liability regime for in-scope companies does **not fully respect EU civil law principles**, since it does not refer to the rules of civil liability which could give right to compensation i.e., an unlawful (intentional or grossly negligent) conduct by the company in breach of the failure to comply with the due diligence requirements, an actual and real damage occurred and a causal link between them. Also, companies should not be exposed to liability risks when they **could only have identified** the potential for an adverse impact **but could not have prevented** the resulting adverse impact or damages. Companies should not be held liable for the conducts of non-controlled subsidiaries. This provision should be **redrafted as to be in line with civil law principles and to not expose companies to unjustified excessive litigation.**

➢ **Rules on directors' duties need to be revised or deleted**

Provisions on directors' duty of care are **not clear and impose overarching general policy objectives** upon directors, actionable (in principle) by any "stakeholder". They will have a negative impact on companies' competitiveness, by creating risk aversion, slowing down decision-making processes, increasing legal and administrative costs and impairing recruitment of skilled individuals. These provisions should be therefore **deleted or revised**.

III. Legal assessment and key messages in detail

a) The material scope of the due diligence obligations should be revised to achieve proportionality of measures and effectiveness on the ground

Article 1 sets out the **subject matter** of the Directive by laying down rules on obligations of due diligence for companies regarding **actual and potential human rights and environmental adverse impacts** with respect to **value chain operations**. It covers companies' own operations and operations of their controlled subsidiaries, as well as the entire value chain encompassing established (direct and indirect) business relationships, both upstream and downstream.

Considering our globalized economies and the complexity of commercial relations, it is undoubtedly unrealistic to consider that a company can effectively control its entire value chain, especially its indirect upstream and (more importantly) indirect downstream operations and business partners. Due diligence obligations as proposed are not reasonable nor workable and companies should not be held responsible for events that are out of their control, such as continuing violations of human rights in countries where local authorities do not apply EU-like protection standards. In addition to the above difficulties, it is very likely that many foreign companies based in non-EU countries will not facilitate access to information. The Proposal presupposes that European companies can in fact exert their influence on their business partners, which is evidently not always the case. Especially in third countries where protection standards are not the same as in the EU, certain business partners are more powerful than their clients and they may also be under State control. As long as foreign governments do not align with EU protection standards for Human Rights and the Environment, it could not be reasonably expected that

their companies will abide by them on an individual basis. Even the concept of "value chain" may be interpreted differently in different sectors of activities and in different jurisdictions.

It is therefore recommended that the ***concept of chain(s)*** *be further clarified to avoid discordant interpretations across the MS. It may be expected that companies will have to limit the number of suppliers to be able to conduct their due diligence more cost-effectively and securely. As a result, the risk of concentration of suppliers could lead to further price inflation and shortages. The Directive's obligations and their scope should be re-considered on that basis and alternatively, a more targeted due diligence regime should be introduced, based on the most relevant adverse impacts, in respect of certain products and not any activity of the in-scope company.*

The text of the Directive should be rephrased to ensure that due diligence obligations are ***feasible****, and their scope does not extend to the whole value chain but* ***to companies' first-tier direct supplier(s)*** *(i.e., those parts of the supply chain with which companies have* ***a direct contractual relationship), in compliance with the principle of proportionality****. Moreover,* ***companies' downstream operations should be excluded***[2]*.*

Finally, the scope needs to ***ensure the level playing field between EU and non-EU companies.*** *The Proposal* ***does not make any distinction between operations in the EU and operations outside of the EU.*** *This does not reflect the reality, given that human rights and environment protection standards are higher in the EU than outside of the EU.* ***This reality should be duly taken into consideration and the efforts of EU businesses acknowledged****. The due diligence obligations should be tailored around this fact to fulfil the ambition of the Commission and the business world for an immediate elevation of protection standards, without additional costs for companies that are already aligned with EU standards.*

b) Revisiting the personal scope of the Directive to ensure level playing field and optimal harmonisation of provisions

Article 2 establishes the personal scope of application of the Proposal. Notably, it applies to:

- EU companies with more than 500 employees and net worldwide turnover of above 150 million EUR.
- Other EU companies between 251-500 employees and net worldwide turnover of above 40 million EUR out of which at least 50% generated in one or more specific high-risk sectors (agriculture and food, mining, garment and footwear, new: forestry and fishing, etc.).
- Non-EU companies within the above thresholds but with the relevant turnover being generated within the EU market.

SMEs are not included in the direct personal scope of the Directive.

Firstly, the Proposal does not provide a true level playing field in relation to non-EU companies, since the thresholds for non-EU companies are much higher than those provided for EU companies. Consequently, EU companies falling within the scope of the Proposal will likely be much smaller than non-EU companies. We

[2] Considering, for example, the industrial sector, it is expected that a company can only exert a relative influence on direct suppliers, while influence on indirect suppliers that might be marginal at best.

therefore suggest changing the turnover criteria, so that for both EU and non-EU companies the relevant turnover is calculated on what is generated within the EU.

Secondly, the Proposal includes a very broad list of high impact sectors and covers everything produced within a sector irrespective of whether the actual product or service can have a high impact on human rights and environment. This might cause a particularly strong inflation of prices of related raw materials and products. We therefore think that the Directive should either limit the list of high impact sectors to certain parts of sectors, limit within different stages of production as not all stages nor types of products present significant risk for human rights and the environment or work with lists of products with high impact codes, for example the HS codes used in the Combined Nomenclature. This would be also in line with a more targeted, risk-based, approach as explained under III. a) above.

As to SMEs, we welcome their exclusion. However, they will be indirectly affected as suppliers in the supply chain because of the actions taken by the bigger companies to comply with the Directive's obligations. SMEs will therefore face challenges and contractual constraints, notably through contractual cascading mechanisms. This will imply costs of implementation and unnecessary bureaucracy and burdens for SMEs, which should be avoided or, at least, mitigated inter alia with appropriate accompanying measures.

The Proposal leaves too much discretion to MS to legislate, which could eventually lead to fragmentation of rules withing the internal market. The Directive should ensure targeted full harmonisation to deliver a level playing field among MS by avoiding fragmentation of internal market rules and ensuring uniform rules and standardisation. At least key provisions, especially those imposing obligations and requirements related to due diligence plans, reporting and information sharing obligations and liability, should be fully harmonised and coherent.

On the face of it, the due diligence obligations established are set at company level and not at group level. Whilst we understand the reasons for this choice, the challenges for groups of companies de facto exposed to different national rules within the single market must be addressed. The current Proposal would be practically difficult and burdensome for companies to handle, and it would lead to inconsistent applications between companies within the same group. Groups of companies should have the flexibility to organise their due diligence plans according to their business model, thereby avoiding fragmentation of approaches and enhancing the effectiveness of due diligence strategies and actions within groups.

c) Certain definitions should be revised and clarified

Article 3 contains definitions for the purpose of this Directive. In addition to our comments on the notion of "value chain" above, the following definitions should be revisited.

<u>Definitions of "business relationship" and "established business relationship"</u>

A business relationship is defined as a relation with a (sub)contractor or any other legal entity with whom the company has a commercial agreement, or which performs business operations related to the products or services of the company, for or on behalf of the company.

An established business relationship is defined as 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.

We consider that these definitions are very broad and unclear, which makes it impossible to identify what is an established business relationship. It is also to be noted that these definitions do not address the issue of certain grey areas of the supply chain, such as traders in between the chain. Moreover, such unclarity would create a substantial risk that MS interpret and apply these definitions differently. These concepts need to be clearly defined and "established business relationships" should be limited to first-tier suppliers only.

Definition of "stakeholders"

"Stakeholders" are defined as the company's employees, the employees of its subsidiaries, and other individuals, groups, communities or entities whose rights or interests are or could be affected by the products, services and operations of that company, its subsidiaries and its business relationships.

This definition is too broad, considering that obligations on companies concerning "stakeholders" are many and significant. For example, stakeholders need to be consulted by the companies when assessing actual and potential adverse impact (Article 6), they can submit complaints to the companies (Article 9) and provide input regarding the companies' due diligence policies (Article 26), and stakeholders can claim damages under the civil liability provision (Article 22).

It is therefore recommended that alternative definitions of stakeholder be considered. For example, a stakeholder could be defined as a person who has specific attributes which pertain to them or by reason of circumstances that differentiate them from all other persons and who has a specific and actual (or soon to occur) injury that is causally connected to the conduct complained[3]*.*

The notion of "appropriate measures"

The Proposal does not provide sufficient guidance for companies as to what is "reasonable" or not and considering that the company's "influence" is to be taken into account when assessing whether a measure is "appropriate" or not, it still remains unclear which measures allow companies to comply with their due diligence obligations.

d) Need for legal certainty, effectiveness and enforceability of due diligence obligations and the importance of standardisation

Article 4 establishes that MS must ensure that companies conduct human rights and environmental due diligence by complying with the specific requirements listed in Articles 5 to 11 of the Directive.

[3] See judgment of the Court of 15 July 1963, *Plaumann & Co. v Commission of the European Economic Community*, case 25-62, ECLI:EU:C:1963:17.

The Proposal builds on UN's Guiding Principles on Business and Human Rights and OECD Guidelines for Multinational Enterprises and responsible business conduct.

When transposing those concepts into a mandatory legal instrument as the Directive at hand, appropriate adjustments are necessary in order to ensure that the relevant provisions are in fact applicable; the passage from voluntary to mandatory legal instruments requires more attention. The Directive does not provide companies with appropriate guidance to be in position to ascertain whether their due diligence plan is compliant or not (e.g., level of detail of the plan, actual conduct of the due diligence exercise, conditions for reliance on confirmations for compliance requested and received).

The Directive is also vague as regards the form, content and placement of the due diligence policy and of the statement to be published by the in-scope companies. For example, should the "statement" referred to in Article 11 (Communicating) include the due diligence policy referred to in Article 5 and/or any other element? Should the due diligence policy be integrated into the articles of association of a company, or should it be in a separate document? It is important to clarify the above, considering that the legal consequences attached to the due diligence policy and/or statement in question may vary.

In addition to Commission's guidelines, companies should be allowed to have recourse to standardisation scheme such as unified labelling or certification systems based on common standards and delivered by certified bodies.

Article 5 requires MS to ensure that companies integrate due diligence into their corporate policies including a code of conduct for employees and subsidiaries. They must keep them under review and up to date annually. Companies will be required to take "appropriate measures" to identify (Article 6), prevent or adequately mitigate (Article 7) and bring to an end or minimise the extent (Article 8) of potential or actual adverse impacts arising from their own operations, those of their subsidiaries and those of the entities.

The "appropriate measures" will have to be commensurate with the degree of severity and the likelihood of the adverse impact, and reasonably available to the company. Those measures will therefore vary on a case-by-case basis, which creates uncertainty for companies and may result in significant expenses and administrative burdens for them.

The Directive fails to address the issue relating to the plethora of codes of conducts and plans that SMEs will be required to comply with, as part of the value chains of in-scope companies.

The text also requires in-scope companies to ensure compliance with their plans and codes of conduct, which is also a condition for benefiting from the exemption of civil liability in case of indirect business partners. Achieving compliance with the company's code of conduct will not be always possible, and in most cases, it will be simply impossible to impose upon a business partner. Hence, exemptions from liability should be set out around this element.

Additionally, Article 8(6) of the Proposal provides that, if all other measures have failed, the company shall refrain from entering into new or extending existing relations with the partner in connection to or in the value

chain of which the impact has arisen and shall, where the law governing their relations so entitles them to, take one of the following actions:

(a) temporarily suspend commercial relations with the partner in question, while pursuing prevention and minimisation efforts, if there is reasonable expectation that these efforts will succeed in the short term;

(b) terminate the business relationship with respect to the activities concerned if the potential or actual adverse impact is severe.

MS will have to provide for the availability of an option to terminate the business relationship in contracts governed by their laws.

These provisions violate the freedom to conduct business and the scope of guaranteed rights under the EU Charter of Fundamental Rights[4]. In addition, such prescriptive provision may even be counter-productive for the achievement of the Proposal's objectives to elevate human rights and environment protection standards in third-country jurisdictions where most of violations occur.

It should be also clarified what happens when the law applicable to a contract is not that of a MS and what are the options left for EU companies to avoid incurring liability in these cases.

Furthermore, MS will have to ensure that companies establish a process for submission of complaints by affected persons, trade unions or workers' representatives and civil society organisations in relation to companies concerns regarding those potential or actual adverse impacts, including in the company's value chain (Article 9).

Cost of implementation of the process is expected to be high, given the rights granted to complainants.[5] Additionally, the risk of abuse of the complaints mechanism should be duly considered as well as procedural safeguards (confidentiality of information and documents made available to parties, modalities, etc.).

Also, MS are to provide that companies periodically assess the effectiveness of their own operations and measures, including those of their subsidiaries and those entities in their value chain, in connection with the Directive's obligations (Article 10).

It is not clear how such monitoring could be ensured as regards third-country entities being part of the value chain. Additional costs for businesses are to be expected in connection with the requisite risk assessment and regular re-assessment provided for under the Directive.

[4] Article 16 of the EU Charter of Fundamental Rights.
[5] For example, Article 9(4) Member States shall ensure that complainants are entitled:
(a) to request appropriate follow-up on the complaint from the company with which they have filed a complaint pursuant to paragraph 1, and
(b) to meet with the company's representatives at an appropriate level to discuss potential or actual severe adverse impacts that are the subject matter of the complaint.

Lastly, considering the far-reaching due diligence obligations, the co-legislators should pay particular attention to the costs to be borne by both directly and indirectly impacted companies, such as the audit costs and those related to independent third-party verifications which in the current version of the Proposal should be borne by in-scope companies entering in business relationships with SMEs.

e) Model contractual clauses should be developed together with business

Article 12 states that to provide support to companies to facilitate their compliance with certain obligations of the Directive[6], the Commission will have to adopt guidance about voluntary model contract clauses.

We welcome this provision. However, we consider that model contractual clauses should be developed in collaboration with businesses, including with SMEs, which will be the parties affected in the implementation of the Directive. We also recommend that such clauses become available as soon as possible and before the transposition deadline to leave time to companies to implement them.

f) Accompanying measures need to be guaranteed

Pursuant to article 14, MS and the Commission will have to provide accompanying measures to companies and to other actors along global value chains indirectly impacted by the Directive. Such support can range from the operation of dedicated websites, portals or platforms to financial support to SMEs, and facilitation of joint stakeholder initiatives. This provision further clarifies that companies may rely on industry schemes and multi-stakeholder initiatives to support the implementation of due diligence and that the Commission, in collaboration with MS, may issue guidance for assessing the fitness of such schemes.

As a preliminary comment, it is noted that the measures introduced by the proposal are neither sufficient nor appropriate for the due diligence exercise imposed on companies for their entire value chain. The fact that those measures merely "can" or even "may" be introduced, leaves open the risk that the Directive, if adopted as proposed, will not facilitate in any way the introduction of these measures in favour of companies to support their implementation of the Directive.

It is therefore recommended that common EU rules be introduced to provide for precise accompanying measures. Moreover, it is also recommended that the accompanying measures further recognise existing sectoral standards. As regards industry schemes and multi-stakeholder initiatives, the Commission should publish a list of those schemes and initiatives on which companies can rely on to support the implementation of due diligence obligations under the Directive. The Commission, in collaboration with MS, should assess on an annual basis the fitness of industry schemes and multi-stakeholder initiatives and where appropriate, update the list. On this note, we consider that the Commission should have a prominent and centralised role in granting companies the information and support they need[7].

[6] Article 7(2), point (b), and Article 8(3) point (c).
[7] See in this respect also BusinessEurope's position paper on Corporate Sustainability Due Diligence proposal dated 31 May 2022.

A presumption of compliance of the company which adheres to these standards should be included in the Directive[8].

g) Obligations on climate change should not be included in the Directive

Article 15 requires MS to ensure that EU companies above 500 employees and non-EU companies with a turnover of EUR 150 million adopt plans to ensure that their business model and strategy 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. Those companies will therefore have additional obligations by assessing the extent to which climate change is a risk for, or an impact of, their operations (Article 15(1)). If risks are, or should have been, identified, they will have to include emission reduction objectives in their plans (Article 15(2)). Furthermore, the Proposal requires that the variable remuneration of directors is linked to their contribution to the company's business strategy and long-term interests and sustainability (Article 15(3)).

As a preliminary note, it is to be considered that the Paris Agreement and the objective of climate-neutrality by 2050, which are fully supported by Luxembourg business, are reflected in a plethora of legislative initiative at EU and national level[9]*. We therefore consider that Article 15, if adopted as proposed, would only create inconsistencies with already existing legislation, while adding further obligations that are not related to the main purpose of the Proposal, which concerns due diligence and not climate change. Furthermore, we believe that this provision leaves too much discretion to MS to interfere with corporate governance models and will fragmentate even further the rules adopted within the EU.*

We recommend that this provision be deleted from this Directive, so that this issue can be properly dealt with by the other legislative instruments dedicated to it. In the alternative, we advocate that this provision is revised as to not pose an obstacle to the existing legislation on the matter.

Finally, the issue relating to the directors' variable remuneration is already dealt with in the Shareholders Rights Directive which contains rules on pay in listed companies, coupled with the various national corporate governance codes imposed and enforced by national financial markets watchdogs[10]*.*

h) Sanctions and enforcement are not proportionate and lack guarantees

Articles 17 and 18 of the Proposal establish that MS have to designate one or more national supervisory authorities with a minimum set of enforcement and investigation powers. Article 19 requires MS to ensure that natural and legal persons are entitled to submit substantiated concerns to any supervisory authority when they have reasons to believe, based on objective circumstances, that companies did not comply with the national provisions adopted pursuant to the Directive. Moreover, according to Article 20, MS are required to lay down

[8] See in this respect also Eurochambres' position on the Proposal for Corporate Sustainability Due Diligence.
[9] It should be noted that this Proposal is a component of the European Green Deal and it complements other legislative initiatives like the 'Fit-for-55' package, the Corporate Sustainability Reporting Directive, the Sustainable Finance Disclosure Regulation and the Taxonomy regulation.
[10] See « Les X principes de gouvernance d'entreprise de la Bourse de Luxembourg », containing a series of extensive rules applicable to all listed entities in Luxembourg (national and foreign).

rules on effective, dissuasive and proportionate sanctions for breaches of the national provisions adopted pursuant to the Directive, and to take all measures necessary to ensure that they are implemented. When pecuniary sanctions are imposed, they will be based on the company's turnover, and they will be published. Account will be taken of the company's efforts to comply with any remedial action required of them by a supervisory authority. Finally, Article 24 establishes that companies breaching the Directive's obligations can be deprived from public support.

We consider that the national supervisory authorities' powers are too intrusive and disproportionate and not appropriately counter-balanced with due process and appeal rights[11]. We recommend that Articles 17 to 20 be revised as to ensure the proportionality and the due process rights in relation to sanctions and enforcement.

Moreover, the Proposal does not specify whether pecuniary sanctions are based on the total global or EU turnover or the turnover in the country in which the sanctioned conduct took place, or in the country of the legally registered head office (Article 20(3)). This element needs clarification to ensure legal certainty and foreseeability.

As to the deprivation of public support, on the one hand, we consider that the concept of "public support" is vague, as it lacks a definition, which will lead to legal uncertainty and to fragmentation of rules within the MS. On the other hand, we flag that this provision could violate fundamental principles of law insofar as it might lead to double punishment for the same facts (ne bis in idem), it leaves companies open to eternal punishment given that it does not contain any time limitation, it is not proportionate as it does not refer to the severity or nature of the breach, it gives. This provision should thus be redefined taking into account the above considerations or deleted.

On a different note, it should be noted that it is not clear how sanctions could reasonably be enforced on non-EU companies, especially since the Proposal establishes that the sanctions are set by MS and, as such, they are expected to differ across the MS.

Public enforcement powers should be harmonised across MS to avoid fragmentation of rules and to ensure a level playing field within the EU. The Directive should therefore provide for more detailed rules regarding the set-up of supervisory authorities and their powers.

Furthermore, it is necessary that the Directive ensure coordination among the different MS supervisory authorities, especially in the case where more than one companies from the same group are established in

[11] Reference is made in particular to:
- The power to request information and carry out investigations related to compliance with the obligations set out in the Directive.
- The power to initiate an investigation on their own motion or because of substantiated concerns.
- The possibility to conduct inspections without prior notification to the company concerned.
- The power to order the cessation of infringements of the national provisions, abstention from any repetition of the relevant conduct and, remedial action proportionate to the infringement and necessary to bring it to an end.
- The power to impose pecuniary sanctions.
- The power to adopt interim measures.

different MS To this end, the Directive could provide for the establishment a central authority overseeing its implementation across MS.

We further recommend that MS be aligned as regards the relationship between the severity of an offence and the sanctions applied by the competent authorities, to avoid fragmentation of rules and to ensure a level playing field within the EU and with regards to non-EU companies when it comes to enforcement.

Lastly, the competence of the supervisory authorities concerning substantiated concerns 19 that can be brought before a supervisory authority as referred to in Article appears unlimited as it refers to any breach of the Directive's obligations. This is too broad. Consequently, any external stakeholder could bring a case before a supervisory authority. We consider that only directly affected parties or entities with legitimate interest should have the right to file substantiated complaints and that such complaints should only refer to potential breaches of companies' due diligence obligations.

i) Liability for damages or civil liability

Article 22 prescribes that MS establish rules on companies' civil liability for damages arising for failure to comply with the due diligence obligations. The civil liability of companies will be without prejudice to the civil liability of their subsidiaries or of any direct and indirect business partners in the value chain.

On the basis of the Proposal, the conditions under which the above regime will be triggered have not been drafter in a sufficiently precise manner and therefore it is not clear whether they are aligned with civil law principles (i.e., an unlawful (intentional or grossly negligent) conduct by the company, failure to comply with specific legal requirements, an actual and real damage occurred and a causal link between them).

As explained above, the obligations imposed upon in-scope companies, the measures they should take in order to fulfil them and the adverse impacts relating to the due diligence exercise are vaguely ascribed in the Directive.

As far as the notion of "appropriate measures" is concerned, in-scope companies should take the "appropriate measures" which can reasonably be expected to result in prevention or minimization of the adverse impact under the circumstances of the specific case. Appreciation on whether the measures taken by the company are "appropriate" or not, shall take into account the following elements:

- *specificities of the company's value chain;*
- *sector or geographical area in which the value chain partners operate;*
- *company's power to influence its direct and indirect business relationships;*
- *whether the company could increase its power of influence.*

Nonetheless, the Proposal does not provide further specific guidance as to the way the above elements could be assessed by the companies and then verified. Associating liability to vague obligations without proper practical guidance for companies is disproportionate.

As the Proposal currently stands, it is particularly concerning that the possibility that companies face liability lawsuits in those cases where they could only have identified the potential for an adverse impact but could not have prevented the adverse impact or the damages resulting from it.

Furthermore, it is equally worrying that companies can be liable for unlawful conducts of non-controlled subsidiaries or entities on which they have no influence and therefore upon which it is extremely difficult (if not impossible) to impose their internal codes of conduct (or in general, the measures that they are required to enforce according to the Directive). The legal liability regime relating to due diligence as introduced by the Proposal should take stock of such reality.

This provision is unclear, and potentially breaches the proportionality principle, exposing companies to unjustified excessive litigation. We therefore call upon the co-legislators to clarify the civil liability provision and to redraft it as to correct the above shortcomings.

j) Rules on directors' duties need to be revised or deleted

Article 25 deals with directors' duty of care. It requires MS that their national legislation ensure that companies' directors take into account the consequences of their decisions for sustainability matters, including human rights, climate change and environmental consequences in the short, medium and long term. Article 26 establishes that directors are responsible for putting in place, overseeing and adapting their companies' due diligence policies and actions with due consideration for relevant input from stakeholders and civil society organisations. The directors will also have to report on this to their boards.

These provisions are not clear and impose overarching general policy objectives upon directors, without however providing them with the necessary tools and guidance to this effect.

We are concerned that they will have an arbitrary and unjustified interference over the management of companies and overly complexify the already difficult exercise of decision-making of directors. In addition, the management bodies of EU companies integrate already into their decision-making processes all relevant stakeholders' interests, such that article 25 does not have any added value in this respect.

The Proposal simply exposes directors to liability vis-à-vis third parties for their management decisions, without taking into consideration that balancing conflicting interests is an extremely difficult task, the proposed rules contribute to creating risk aversion, slowing down decision-taking processes, increasing legal, administrative and insurance costs and impairing recruitment of skilled individuals.

We therefore recommend deletion of article 25 and revision of article 26, in order to reflect that the text of the Proposal already requires that stakeholders are consulted during, and for the purposes of, implementation of due diligence obligations and in order to exclude personal liability of directors towards third parties.

CHAMBER OF COMMERCE LUXEMBOURG

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Joint position paper
on Corporate Sustainability Due Diligence

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