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Study on due diligence requirements through the supply chain

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British Institute of International and Comparative Law

CIVIC CONSULTING

THE LONDON SCHOOL OF ECONOMICS AND POLITICAL SCIENCE

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ABSTRACT

This study for the European Commission focuses on due diligence requirements to identify, prevent, mitigate and account for abuses of human rights, including the rights of the child and fundamental freedoms, serious bodily injury or health risks, environmental damage, including with respect to climate. It was conducted by the British Institute of International and Comparative Law (lead), Civic Consulting and LSE Consulting. Through desk research, country analyses, interviews and surveys it identifies Market Practices (Task 1) and perceptions regarding regulatory options. The Regulatory Review (Task 2), including twelve Country Reports, shows that UN Guiding Principles on Business and Human Rights' standard of due diligence is increasingly being introduced into legal standards or proposed in Member States. The Problem Analysis, policy background and intervention logic concludes with the definition of four options for regulatory proposals (Task 3): No change (Option 1), new voluntary guidelines (Option 2), new reporting requirements (Option 3) and mandatory due diligence as a legal standard of care (Option 4). Option 4 includes sub-options limited to sector and company size, and enforcement through state-based oversight or judicial / non-judicial remedies. The assessment of impacts of regulatory options (Task 4) considers economic impacts, impacts on public authorities, social, human rights and environmental impacts.

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EXECUTIVE SUMMARY (English)[1]

1. Background

This is a study for the European Commission DG Justice and Consumers on due diligence through the supply chain, undertaken by the British Institute of International and Comparative Law (BIICL) in partnership with Civic Consulting and LSE Consulting.

The mandate for this study derives from Action 10 of the European Commission Action Plan on Financing Sustainable Growth of 8 March 2018,[2] to:

> [C]arry out analytical and consultative work with relevant stakeholders to assess: (i) the possible need to require corporate boards to develop and disclose a sustainability strategy, including *appropriate due diligence throughout the supply chain*, and measurable sustainability targets; and (ii) the possible need to clarify the rules according to which directors are expected to act in the company's long-term interest. [Italics added]

The mandate further derives from the May 2018 European Parliament Report on Sustainable Finance, which calls for a "legislative proposal" for "an *overarching, mandatory due diligence framework including a duty of care* to be fully phased-in within a transitional period and taking into account the proportionality principle". [3]

The concept of due diligence relevant to this study, to "identify, prevent, mitigate and account for" adverse corporate impacts on human rights and the environment, was introduced by the UN Guiding Principles on Business and Human Rights ("UNGPs"),[4] and incorporated into the OECD Guidelines for Multinational Enterprises ("OECD Guidelines")[5] to extend to other areas of responsible business conduct such as the environment and climate change, conflict, labour rights, bribery and corruption, disclosure and consumer interests,[6] as well as in the ILO Tripartite declaration of principles concerning multinational enterprises and social policy ("MNE Declaration").[7] It is also the foundation for the French Duty of Vigilance Law, which requires "reasonable *vigilance measures" as a standard of care* for human rights and environmental harms, and which the European Parliament report states should be the *basis for the "pan-European framework"*.

This study is an initial study for the possible development of regulatory options at the EU level.

2. Market Practices (Task 1)

The methodology for the collection of evidence on market practices consisted of surveys, interviews, case studies, and desktop and legal research of relevant materials.

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[1] For brevity, this Executive Summary summarises the content of the study with only limited footnoted references. For references, please see the Main Report or Synthesis Report.
[2] Action 10 of the Communication from the Commission to the European Parliament, the European Council, the Council, the European Central Bank, the European Economic and Social Committee and the Committee of the Regions Action Plan: Financing Sustainable Growth, COM/2018/097 final, 8 March 2018.
[3] European Parliament Report on Sustainable Finance, 2018/2007(INI) at para 6.
[4] UN Office of the High Commissioner for Human Rights "Guiding Principles on Business and Human Rights: Implementing the 'Protect, Respect and Remedy' Framework" ("UNGPs"), HR/PUB/11/04, 2011.
[5] OECD Guidelines on Multinational Enterprises, 2011
[6] OECD Guidelines ibid Commentary on General Policies at para 14.
[7] ILO, Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy, Adopted by the Governing Body of the International Labour Office at its 204th Session (Geneva, November 1977) and amended at is 279th (November 2000), 295th (March 2006) and 329th (March 2017) Sessions ("MNE Declaration").

The 334 business survey respondents ranged from all sectors, and represented enterprises of all sizes. Business respondents operated across the EU and the world, with only 15.32% of respondents indicating that they only operate within the EU, and at least 40 respondents operating in each Member State.

The 297 general survey respondents (including business associations and industry organisations, civil society, worker representations or trade unions, legal practitioners and government bodies) similarly provided a representative and balanced sample. General survey respondents indicated that their work covers all sectors and company sizes. The largest group indicated that their work is not sector-specific or that it spans across sectors. All EU Member States were selected by general survey respondents as being relevant to their work.

Just over one-third of business respondents indicated that their companies undertake due diligence which takes into account all human rights and environmental impacts, and a further one-third undertake due diligence limited to certain areas. However, the majority of business respondents which are undertaking due diligence include first tier suppliers only. Due diligence practices beyond the first tier and for the downstream value chain were significantly lower. The vast majority of business stakeholders cover environmental impacts, including climate change, in their due diligence, although the term "climate change due diligence" for a self-standing process is currently rarely used, and human rights and climate change processes often take place in "silos".

The most frequently used due diligence actions include contractual clauses, codes of conduct and audits. Divestment was the least selected due diligence action by both business and general respondents.

When asked about the primary incentives for undertaking due diligence, business respondents and industry organisations selected the same top three incentives as being: reputational risks; investors requiring a high standard; and consumers requiring a high standard. Presumably because of the existing lack of regulatory or legal requirements to undertake due diligence, business and industry organisation respondents indicated that regulation or legal requirements are currently, or have been in the past, the least selected incentives for companies to undertaking due diligence. In contrast, general stakeholders and civil society respondents viewed regulatory incentives as the top incentives for due diligence.

Survey respondents indicated that the current legal landscape (Option 1) does not provide companies with legal certainty about their human rights and environmental due diligence obligations, and is not perceived as efficient, coherent and effective.

Interviewees across business and other stakeholders agreed that there is already enough voluntary guidance (Option 2) in existence, and survey respondents overall seemed unconvinced that new voluntary guidance would have notable social, environmental and human rights impacts. In contrast, survey respondents from industry organisations expressed a preference for voluntary guidelines, drawing attention to the influential nature of existing soft law mechanisms. Stakeholders however suggested that voluntary guidance could be helpful to supplement and clarify any legal obligations, particularly relating to the specificities of certain sectors or issues.

Survey respondents were more positive about the likely sustainability impacts of new regulatory reporting requirements (Option 3). Perceived shortcomings stated by survey respondents were that reporting requirements do not usually provide for effective sanctions for non-compliance, and do not substantively require appropriate due diligence for compliance with the regulatory obligation. It was nevertheless highlighted that reporting requirements in this area have had a positive impact in raising awareness, and that some are relatively new.

The majority of stakeholders indicated that mandatory due diligence as a legal standard of care (Option 4) may provide potential benefits to business relating to harmonization, legal certainty, a level playing field, and increasing leverage in their business relationships throughout the supply chain through a non-negotiable standard. The level playing field and legal certainty were amongst the most important considerations for business interviewees, whereas general interviewees highlighted its potential to address the lack of access to remedies for affected parties and improve implementation of due diligence. Almost all interviewees were in principle in favour of a policy change to introduce a general standard at the EU level, although they differed on aspects of liability and methods of enforcement. However, industry organisation survey respondents were overall not in favour of the introduction of new policy changes, including mandatory due diligence.

Within this option, the overall preference appears for a general cross-sectoral regulation, but which takes into account the specificities of the sector, and the size of the company in its application to specific cases. Survey respondents expressed an overall preference for a standard which applies regardless of size, but views varied in this respect: many noted a concern about the potential burden for SMEs, whilst other argued that many of the risks in their supply chain relate to the activities of SMEs.

Stakeholders further indicated that the legal mechanism should be based on a standard of care rather than a procedural (frequently described as "tick box") requirement, and they indicated that a company should be able to avoid legal liability by showing that it has undertaken the due diligence required in the circumstances (the due diligence defence). Interviewees also highlighted that mandatory due diligence laws should form part of a "smart mix" of measures. Some stakeholders remarked that a transitional period would be helpful. A few interviewees indicated that an EU-level regulation linked to legal requirements for operating in or access to the European market would be a powerful incentive. Many stakeholders emphasized the global importance of the EU leadership in this area.

It is also noted that, increasingly, individual multinational companies support the introduction of mandatory due diligence regulation, although there is no agreement on the form of liability and enforcement mechanisms. In contrast, the majority of industry organisation survey respondents appear to be in favour of the least enforceable regulatory options. In this respect, industry organisation's views on regulatory options are contradictory to those of individual multinational companies on some of these key questions.

Stakeholders across the spectrum seemed to be in consensus, with many expressing strong views, that the UNGPs concept of due diligence should not be abandoned for something that is more "vague". Instead, stakeholders suggested that any regulatory mechanism should build upon the influence and strength of the due diligence concept of the UNGPs.

3. Regulatory Review (Task 2)

The study reviewed the regulatory framework applicable to due diligence for human rights and environmental impacts internationally, in the EU as well as in some non-EU jurisdictions, and in 12 selected Member States through Country Reports by legal experts.

The UNGPs state that in order to meet their responsibility to respect human rights, business enterprises should carry out human rights due diligence[8] to "identify, prevent, mitigate and account for"[9] actual or potential adverse human rights impacts a company may be involved in through its own activities or business relationships. This responsibility applies regardless of size, sector or where the company operates.[10] The UNGPs refer to the value chain (not the supply chain),[11] and extends the responsibility to those impacts that "the business enterprise may *cause* or *contribute to* through its own activities, or which may be *directly linked* to its operations, products or services by its business relationships".[12] The concept of leverage is used to determine whether the company has taken "appropriate action" in circumstances where it may contribute or be directly linked to an impact.[13] Leverage is "considered to exist where the enterprise has the ability to effect change in the wrongful practices of an entity that causes a harm".[14] The UNGPs state that human rights due diligence should be ongoing (not once-off), context-specific (not a one-size fits all "tick-box"), and cover all human rights,[15] although certain risks may be prioritised based on severity.[16] Risks should be defined as risks to rights-holders (i.e. people and the planet), thereby extending beyond risks to the company.[17]

The influence of the UNGPs is evident in the widespread adoption of the concept and terminology of due diligence in other subsequent standards. For example, the OECD Guidelines for Multinational Enterprises,[18] were revised in 2011 to align with the UNGPs,[19] and its guidance on Responsible Business Conduct incorporates a similar standard of due diligence as the UNGPs, including application "in all stages of the supply chain or value chain".[20] The OECD Guidelines extend the concept of due diligence expressly to other areas of responsible business conduct, including environment and climate change, as well as risks related to conflict, labour rights, bribery and corruption, disclosure and consumer interests.[21] OECD member states are required to set up National Contact Points ("NCPs"), to which complaints may be made that a company is in breach of the OECD Guidelines.

The EU has instituted a number of initiatives imposing certain due diligence-related obligations for human rights and environmental impacts, including climate impacts. Sector-specific examples include the EU Timber Regulation ("EUTR")[22] (which predates the UNGPs), as well as the EU Conflict Minerals Regulation,[23] which will come into force on 1 January 2021. The EU has also adopted the EU Non-Financial Reporting Directive,[24] which requires reporting on due diligence, and is accompanied by Non-Binding

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[8] UNGPs 15-21.
[9] UNGP 15.
[10] UNGPs 14 and 23.
[11] UNGP 13 and its Commentary.
[12] UNGP 17.
[13] UNGP 19 and its Commentary.
[14] Commentary to UNGP 19.
[15] UNGP 17 and its Commentary.
[16] Ibid.
[17] UN Human Rights Council, "Report of the Special Representative of the Secretary-General on the issue of human rights and transnational corporations and other business enterprises: 'Protect, Respect and Remedy: a Framework for Business and Human Rights'", A/HRC/8/5, 7 April 2008, at para 6.
[18] OECD Guidelines above n 5.
[19] John Ruggie and Tamaryn Nelson, "Human Rights and the OECD Guidelines for Multinational Enterprises: Normative Innovations and Implementation Challenges", Corporate Social Responsibility Initiative Working Paper No. 66 (May 2015) at 13.
[20] OECD "OECD Guidelines for Multinational Enterprises: Responsible Business Conduct Matters" ("OECD RBC Guidance"), available at: http://mneguidelines.oecd.org/MNEguidelines_RBCmatters.pdf at 61.
[21] OECD Guidelines above n *5*Commentary on General Policies at para 14.
[22] Regulation (EU) No 995/2010 of the European Parliament and of the Council of 20 October 2010 laying down the obligations of operators who place timber and timber products on the market ("EU Timber Regulation").
[23] Regulation (EU) 2017:821 of the European Parliament and of the Council of 17 May 2017 laying down supply chain due diligence obligations for Union importers of tin, tantalum and tungsten, their ores, and gold originating from conflict-affected and high-risk areas ("EU Conflict Minerals Regulation").
[24] Directive 2014/95/EU of the European Parliament and of the Council of 22 October 2014 ("EU Non-Financial Reporting Directive").

Guidelines on non-financial reporting,[25] and the recent Supplement on corporate climate-related information reporting.[26]

Various domestic legislative measures address supply chain due diligence, but they are often sector- or issue-specific. The 2017 French Duty of Vigilance Law[27] is the only legislative example to date which imposes a general mandatory due diligence requirement for human rights and environmental impacts. As this law is new, there are not yet any court judgments to clarify how this law will be interpreted and applied, but the first legal actions have just been instituted.[28] The 2019 Dutch Child Labour Due Diligence Law requires due diligence for child labour,[29] and the 2015 UK Modern Slavery Act[30] requires *reporting on* due diligence for modern slavery and human trafficking. There are also currently pending proposals or campaigns for mandatory human rights and environmental due diligence laws in 13 European countries, including 11 EU Member States. Other existing domestic laws with due diligence requirement include those relating to anti-corruption laws, product safety, public procurement, anti-money laundering, and directors' duties. Due diligence requirements are also contained in the Revised Draft of the UN Business and Human Rights Treaty.[31]

As there is currently no general duty on companies to undertake due diligence for their human rights and environmental harms in most EU jurisdictions, case law has developed various possible avenues to bring claims for adverse human rights and environmental harms in indirect ways, including in tort, criminal law, and consumer protection laws. A few claims to date have been instituted against companies for climate change contributions.

Recent developments are clarifying the content of due diligence requirements for companies' climate change impacts, many of which took place as this study was being undertaken. In particular, in April 2019 the Netherlands OECD National Contact Point for the first time clarified concrete ways in which companies' individual due diligence actions can include targets to address climate change.[32] Reference was made to the relevant company's steps in terms of the Paris Agreement on climate change.[33]

4. Problem Analysis and Regulatory Options (Task 3)

This task consisted of an analysis of the problems, an intervention logic and the identification of the possible regulatory intervention options at EU level.[34]

Option 1: No policy change (baseline scenario)

[25] European Commission, Guidelines on non-financial reporting (methodology for reporting non-financial information) (2017/C 215/01).
[26] European Commission, Guidelines on non-financial reporting: Supplement on reporting climate-related information (2019/C 209/01).
[27] Loi no. 2017-399 du 27 Mars 2017 relative au devoir de vigilance des sociétés mères et des entreprises donneuses d'ordre
[28] See Regulatory Review, section 3.2.6.
[29] *Kamerstukken I*, 2016/17, 34 506, A. See Regulatory Review and Netherlands Country Report.
[30] Section 54 of the UK Modern Slavery Act 2015. See Regulatory Review and UK Country Report.
[31] UN Human Rights Council open-ended intergovernmental working group on transnational corporations and other business enterprises with respect to human rights ("OEIGWG"), "Legally Binding Instrument to Regulate, in International Human Rights Law, the Activities of Transnational Corporations and Other Business Enterprises", 16 July 2019, ("Revised Draft"), available at: https://www.ohchr.org/Documents/HRBodies/HRCouncil/WGTransCorp/OEIGWG_RevisedDraft_LBI.pdf
[32] The Netherlands National Contact Point for the OECD Guidelines for Multinational Enterprises, *Oxfam Novib, Greenpeace Netherlands, BankTrack and Friends of the Earth Netherlands (Milieudefensie) versus ING*, Final Statement, 19 April 2019, available at: https://www.oecdguidelines.nl/documents/publication/2019/04/19/ncp-final-statement-4-ngos-vs-ing.
[33] See Paris Agreement on Climate Change, available at: https://unfccc.int/process-and-meetings/the-paris-agreement/d2hhdC1pcy.
[34] Further considerations identified as relevant to the introduction of a new regulatory intervention are discussed in the full report and include the possibility of accompanying non-binding guidance, the regulation of transnational corporate activity, the application to corporate groups and the supply chain, implementation at Member State level, material scope relating to the definition of human rights and environmental impacts, potential conflict of laws, and a transitional period.

This option would entail no changes in regulation at EU level for companies on undertaking due diligence through the supply chain. It is expected that current national level developments will continue to result in mandatory due diligence legislation in at least some Member States.

Option 2: New voluntary guidelines / guidance

This option would entail new voluntary guidelines at EU level for companies on undertaking due diligence through the supply chain. Voluntary guidelines are by their nature not usually legally enforceable but may influence the standard expected of companies.

Option 3: New regulation requiring due diligence reporting

This option would entail new regulation at EU level requiring companies to report on the steps they have taken to identify, address, prevent and mitigate any adverse human rights and environmental impacts in their own operations or of third-party business relationships (including the supply chain or value chain).[35] This option may differ from the EU Non-Financial Reporting Directive with regard to level of detail and transparency required, and an express focus on risks to people and the planet rather than materiality to shareholders.

Option 4: New regulation requiring mandatory due diligence as a legal duty of care

This option would entail a new mandatory due diligence requirement at EU level which would require companies to carry out due diligence to identify, prevent, mitigate and account for actual or potential human rights and environmental impacts in their own operations and supply or value chain[36], as a legal duty or standard of care. It would allow for a company to demonstrate, in its defence, that it has met this standard by undertaking the level of due diligence *required in the particular circumstances,* i.e. this would be a context-specific risk-based approach. The due diligence standard would allow for prioritisation of those risks which are the most "severe",[37] the "most significant",[38] or the most "salient".[39]

Sub-option 4.1: New regulation applying to a narrow category of business (limited by sector)

This sub-option would entail a substantive legal duty to meet a standard of due diligence, applicable only to a certain sector or commodity.

Sub-option 4.2: New regulation applying horizontally across sectors

In terms of this sub-option, the above new mandatory due diligence regulation (Option 4) would apply across all sectors, either (a) to a defined set of large companies; (b) to all companies regardless of size and so including SMEs, or (c) a general duty for all companies plus an additional duty for large companies only.

Sub-option 4.2(a): applying only to a defined set of large companies

[35] This will depend on the scope of the regulatory intervention. The title of the study in terms of the TOR refers to supply chain but the scope of the mandate described therein envisions an application to the entire value chain. Survey respondents were provided with definitions when asked about details relating to their "upstream supply chain" and "downstream value chain" respectively.
[36] Ibid.
[37] UNGP 17(b).
[38] OECD Guidelines above n 5Chapter II, Commentary at para 16.
[39] Shift and Mazars, "UN Guiding Principles Reporting Framework with implementation guidance", available at: https://www.ungpreporting.org/wp-content/uploads/UNGPReportingFramework_withguidance2017.pdf at 22.

This would entail a general legal duty to undertake due diligence (Option 4), applicable only to a certain defined set of large companies.

Sub-option 4.2(b): applying to all business, including SMEs.

This sub-option would entail a general legal duty to undertake due diligence (Option 4), applicable to all companies, including SMEs.

Sub-option 4.2 (c): general duty applying to all business plus specific additional obligations only applying to large companies

This sub-option is would entail a general due diligence duty applying to all business (including SMEs) plus an additional specific obligation applicable only to large companies. By way of one example, this could take the form of a general due diligence duty applying to all business, (including SMEs), plus an additional obligation linked to climate change targets for large companies.

Sub-option 4.3: Sub-options 4.1 and 4.2 accompanied by a statutory oversight and/or enforcement mechanism

In order to be mandatory, the above new mandatory due diligence regulation (Option 4) would need to be accompanied by an oversight and/or enforcement mechanism. This sub-option considers two sub-sub-options for the enforcement and oversight of such a mechanism, namely (a) through judicial or non-judicial remedies, or (b) through a State-based oversight body and sanctions for non-compliance. These two sub-sub-options are not mutually exclusive and could both apply to the same instrument.

Sub-sub-option 4.3(a): mechanisms for judicial or non-judicial remedies

This sub-sub-option would consist of the above new mandatory due diligence regulation (Option 4) accompanied by mechanisms for judicial and non-judicial remedies for those affected by the company's failure to exercise due diligence.

Sub-sub-option 4.3(b): State-based oversight body and sanction for non-compliance

This sub-option would consist of the above new mandatory due diligence regulation (Option 4) accompanied by a State-based oversight body and sanctions for non-compliance. Oversight and enforcement bodies (often called administrative bodies) can be created at EU and/or Member State level, within existing state departments, or by newly established bodies. Enforcement mechanisms could include fines, the appointment of monitors, withdrawal of licences or trade concessions, or even the dissolution of the company. However, none of these enforcement mechanisms include remedy to the victim, although this could be expressly provided for in addition to the State-based oversight.

5. Assessment of Options

The assessment of the regulatory options was undertaken by LSE Consulting, based on a literature review and an assessment of the survey results. It combines quantitative and qualitative approaches, and aims to discuss and assess, at this preliminary stage,[40] possible costs and benefits of the different regulatory options in the following areas: economic impacts; social impacts; environmental impacts; impacts on human rights;

[40] This is only a preliminary study of regulatory options and not a full-scale impact assessment accompanying a regulatory proposal. As such, the following impact assessment should be taken as a general discussion of potential impacts which could arise if and when a new regulation is designed.

and impacts on public authorities in the EU.[41] It is important to point out that the various stakeholders had different experiences of laws, some of which relate to due diligence reporting and administrative requirements (and not a standard of care). The lack of existing comparative legislative examples resulted in varying expectations among survey respondents.

The quantifications of economic impacts are based on person-day estimates that were given by the surveyed business respondents for each of the four main regulatory options. Generally, businesses' estimates indicate that the number of required person-days, and related costs respectively, would increase moderately with a shift from the status-quo to new reporting requirements, and increase more substantially with a shift from the status-quo to mandatory due diligence. We estimate that the total EU 28 additional annual company-level cost impact (labour cost, overhead and cost of outsourced activities) would be proportionally highest for policy Option 4, with variations depending on company size and sector depending on scope of application.

The impact on competition and innovation is difficult to assess ex-ante. Generally, no significant distortions in intra-EU competition are expected if all companies that operate in the EU are governed by the same set of regulations. While EU companies might be at a relative disadvantage in cost competitiveness compared to non-EU companies, additional firm-level costs as percentages of companies' revenues are relatively low compared to, for example, the applied average tariff for goods imported to the EU. Therefore, no significant negative distortions for EU exporters that result from increased recurrent administrative cost are expected. Business survey respondents expect significant benefits or very significant benefits through decreased distortions, if the new EU regulation creates more equal standards for EU and non-EU suppliers.

Moreover, stakeholders indicated various disadvantages which they experience from the current lack of regulation in terms of the status quo, which they expect to improve if a general duty is introduced at EU level. These benefits include an improvement in competiveness through the levelling of the playing field, so that competitors, peers, suppliers and third parties will be subjected to the same standard, as well as increasing leverage with third parties in the value chain through the introduction of a non-negotiable standard. These benefits are difficult to quantify at this stage, but should be borne in mind, given that they could be significant, and were raised by business stakeholders as one of the most important reasons for the introduction of a mandatory due diligence requirement.

Similarly, business respondents indicated that reputational risk is their top incentive to undertake due diligence under the current status quo. It is expected that these existing reputational risks may be reduced through the introduction of a general due diligence duty. Accordingly, it is likely that the most significant reputational benefits from a mandatory due diligence requirement may result from a reduction in existing reputational risks.

Digitalisation and new technology tools hold the potential to provide unprecedented solutions to identify, address and eliminate human rights infringements and environmental challenges. However, these technological advancements have not been taken into consideration by the vast majority of the respondents.

Cost impacts on public authorities in terms of Options 2 and 3 are expected to remain limited. The additional costs for the monitoring of the implementation of the regulation under Option 4 are expected to be significant, especially if enforcement is to take place

[41] Due to the relative newness of comparable laws which require due diligence as a legal standard of care, it has proven challenging to find impact assessments which have been carried out for similar legislation, and where these were found they did not necessarily include information and/or data which could be used for this analysis.

at Member State or EU level (sub-option 4.3(b)). By comparison, judicial remedies as foreseen in sub-option 4.3(a) are likely to have significantly less additional costs for Member States, insofar as these costs would fall within existing budgets for courts and the judicial system.

Options 2 and 3 are expected to have only a minor positive social impacts. Since these options only provide new guidance or require reporting but do not substantively require companies to take any due diligence measures, it is not expected that substantial additional measures would be taken by companies to address social matters. Both options are also expected not to have any major negative or positive impacts on employment levels. Social impacts from Option 4 are expected to be most significant because the regulatory options require due diligence practices. However, the magnitude and the type of social impacts depends on the design and application of the new regulation, on the social issues which are addressed by the regulation, as well as on the effectiveness of the enforcement mechanisms.

Similarly, the human rights and environmental impacts from Option 4 are expected to be most significant, with positive impacts dependent on proper monitoring and enforcement. However, when comparing Options 2 and 3, respondents foresee voluntary guidelines to be more effective than reporting requirements in delivering positive impacts. The expected positive results are consistent with previous EU assessments.

NOTE DE SYNTHÈSE (Français)[42]

1. Contexte

Cette étude sur le devoir de diligence dans les chaînes d'approvisionnement a été réalisée par le British Institute of International and Comparative Law (BIICL), en partenariat avec Civic Consulting et LSE Consulting, sur requête de la Commission européenne et plus particulièrement de la Direction générale de la justice et des consommateurs.

Le mandat relatif à cette étude émane de l'Action 10 du Plan d'action de la Commission européenne sur le financement de la croissance durable du 8 mars 2018,[43] qui prévoit que:

> La Commission procèdera à des analyses et à des consultations auprès des parties intéressées, pour évaluer: i) l'éventuelle nécessité d'imposer aux conseils d'administration l'obligation d'élaborer une stratégie de croissance durable, prévoyant notamment l'exercice d'une *diligence appropriée tout au long de la chaîne d'approvisionnement*, et des objectifs mesurables en matière de durabilité, et l'obligation de la publier; et ii) l'éventuelle nécessité de clarifier les règles en vertu desquelles les administrateurs sont censés agir dans l'intérêt à long terme de l'entreprise. [Italique ajouté].

Le mandat émane également du Rapport du Parlement européen de mai 2018 sur la finance durable qui invite la Commission à élaborer une « proposition de loi » visant à mettre en place « *un cadre général et obligatoire de diligence raisonnable comprenant un devoir de* vigilance à mettre en place progressivement dans les limites d'une période de transition et en tenant compte du principe de proportionnalité. »[44]

Le concept de diligence raisonnable dont il est fait référence dans le cadre de la présente étude vise un ensemble de procédures permettant aux entreprises d'« identifier, de prévenir, d'atténuer et de rendre compte » des incidences négatives qu'elles peuvent avoir sur les droits de l'homme et sur l'environnement, tel qu'il a été introduit par les Principes directeurs de l'Organisation des Nations Unies relatifs aux entreprises et aux droits de l'homme (« Principes directeurs des Nations Unies »)[45] et intégré dans les Principes directeurs de l'Organisation de coopération et de développement économique (OCDE) à l'intention des entreprises multinationales (« Principes directeurs de l'OCDE »),[46] où il a été étendu à d'autres domaines tels que l'environnement et le changement climatique, l'emploi et les relations professionnelles, la lutte contre la corruption, les pots-de vin et autres formes d'extorsion, et les intérêts des consommateurs, ainsi que dans la Déclaration de principes tripartite sur les entreprises multinationales et la politique sociale de l'Organisation Internationale du Travail (OIT) (« Déclaration de l'OIT sur les entreprises multinationales »).[47] Il constitue également le fondement de la loi française sur le devoir de vigilance qui exige des entreprises la mise en place des « mesures de vigilance raisonnables » en tant que

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[42] À des fins de concision, cette note de synthèse présente un abrégé de la teneur de l'étude et les notes de bas de pages sont limitées. Pour obtenir les références complètes, veuillez vous reporter au Rapport principal ou au Rapport de synthèse.
[43] L'Action 10 de la Communication de la Commission au Parlement européen, au Conseil Européen, au Conseil, à la Banque centrale européenne, au Comité économique et social européen, et au Comité des régions. Plan d'action: financer la croissance durable, COM(2018)97 final, 8 mars 2018.
[44] Rapport du Parlement européen sur la finance durable (2018/2007(INI) au paragraphe 6.
[45] Haut-Commissariat aux droits de l'homme de l'ONU « Principes directeurs relatifs aux entreprises et aux droits de l'homme » mettant en œuvre le cadre « Protéger, respecter et réparer » HR/PUB/11/04 2011
[46] OCDE, *Principes directeurs de l'OCDE à l'intention des entreprises multinationales*, 2011.
[47] OIT, Déclaration de principes tripartite sur les entreprises multinationales et la politique sociale, Adoptée par le Conseil d'administration du Bureau International du Travail à sa 204e session (Genève, novembre 1977) et amendée à ses 279e (novembre 2000) 295e (mars 2006) et 329e (mars 2017) sessions.

norme de conduite, et qui, selon le rapport du Parlement européen, pourrait former le *fondement du « cadre paneuropéen »*.

La présente étude constitue une étude initiale en vue du développement éventuel d'options réglementaires en la matière au niveau européen.

2. Pratiques du marché (Tâche 1)

La méthodologie employée pour cette partie de l'étude a reposé sur des enquêtes, des entretiens et des études de cas, ainsi que sur une recherche documentaire des ressources pertinentes ayant permis d'identifier les pratiques des entreprises en matière de diligence raisonnable.

S'agissant des 334 répondants à l'enquête destinée aux entreprises, ils sont constitués de professionnels provenant d'entreprises de toutes tailles et de tous secteurs d'activité. Ces entreprises exercent des activités à la fois dans l'UE et dans le monde. Seuls 15,32 % des répondants à cette enquête ont indiqué que leurs entreprises ne déploient d'activité qu'au sein de l'UE, et au moins 40 répondants ont indiqué que leurs entreprises déploient une activité dans chacun des États membres de l'UE.

S'agissant des 297 répondants à l'enquête générale, ils sont constitués de membres d'associations d'entreprises et d'organisations industrielles, de membres de la société civile, de représentants des employés ou syndicats, d'avocats et d'organismes gouvernementaux et forment également un échantillon représentatif et équilibré. Ces répondants ont indiqué que leur travail couvre tous les secteurs d'activité et concerne des entreprises de toutes tailles. La majorité des répondants ont précisé que leur travail n'est pas spécifique à un secteur en particulier, mais qu'il englobe plusieurs secteurs. Les répondants à l'enquête générale ont sélectionné tous les États membres de l'UE comme étant pertinents pour leur travail.

A peine plus du tiers des répondants à l'enquête destinée aux entreprises ont indiqué que leurs entreprises mettent en place des procédures de diligence raisonnable couvrant les incidences négatives relatives à l'ensemble des droits de l'homme et l'environnement, tandis qu'un autre tiers a précisé que leurs entreprises limitent leur exercice de la diligence raisonnable à certains domaines particuliers. Une majorité de répondants à l'enquête destinée aux entreprises n'incluent dans leur exercice de diligence raisonnable que leurs fournisseurs de premier rang. Les pratiques en matière de diligence raisonnable allant au-delà du premier rang et incluant les entités situées en aval de la chaîne de valeur sont nettement plus rares. La très grande majorité des parties prenantes issues des entreprises incluent les impacts environnementaux, et notamment ceux liés au changement climatique, dans leurs procédures de diligence raisonnable bien que la « diligence raisonnable en matière de changement climatique » en tant que processus autonome soit rarement utilisée en l'état actuel et que les mesures de diligence raisonnable relatives aux droits de l'homme et celles relatives au changement climatique soient souvent réalisés de manière parallèle.

Les clauses relatives aux droits de l'homme insérées dans les contrats d'approvisionnement, les codes de conduite et les audits figurent parmi les mesures les plus communément mises en oeuvre par les entreprises dans le cadre de l'exercice de leur diligence raisonnable. Le recours au désinvestissement a été la mesure la moins sélectionnée aussi bien par les répondants à l'enquête destinée aux entreprises que par les répondants à l'enquête générale.

Quant aux incitations principales à la mise en oeuvre de mesures de diligence raisonnable, les trois mêmes réponses ont été sélectionnées par les répondants à l'enquête destinée aux entreprises et les organisations industrielles, à savoir, les risques réputationnels, les exigences des investisseurs et les exigences des consommateurs en faveur d'un standard plus élevée. Les répondants à l'enquête destinée aux entreprises et les organisations industrielles ont indiqué accorder une importance moindre aux incitations d'ordre législatives et réglementaires, vraisemblablement en raison du manque d'exigences réglementaires ou législatives en la matière. À l'inverse, les parties prenantes de l'enquête générale et les répondants de la société civile ont considéré que les incitations législatives et réglementaires figuraient parmi les principales motivations de nature à conduire les entreprises à mettre en oeuvre des mesures de diligence raisonnable.

Les répondants aux deux types d'enquêtes ont indiqué que le cadre normatif actuel (Option 1) ne fournit pas aux entreprises de sécurité juridique quant à leurs obligations de diligence raisonnable en matière de droits de l'homme et de l'environnement, et n'est pas perçu comme efficace, cohérent et rationnel.

Les personnes interrogées parmi les entreprises et les autres parties prenantes partagent le point de vue qu'il existe déjà suffisamment de lignes directrices d'ordre volontaire (Option 2) et les répondants à l'enquête ont semblé, de manière générale, peu convaincus que l'élaboration de nouvelles lignes directrices volontaires pourrait avoir des impacts significatifs au niveau social, environnemental et en matière de protection des droits de l'homme. À l'inverse des autres parties prenantes, les répondants issus d'organisations industrielles ont fait part de leur préférence pour des lignes directrices volontaires, attirant l'attention sur le caractère influent des mécanismes existants de droit mou. Un certain nombre de parties prenantes ont suggéré que des orientations volontaires pourraient utilement venir compléter et éclaircir de nouvelles obligations contraignantes en termes de devoir de diligence des entreprises relativement à sa mise en oevre dans le cadre de certains secteurs ou de certains enjeux particuliers.

Les répondants à l'enquête ont été plus positifs à propos des possibles impacts des nouvelles exigences réglementaires en matière de transparence (reporting) (Option 3). Les limitations perçues par les répondants à l'enquête ont permis de comprendre que les exigences actuelles en matière de transparence ne prévoient généralement pas de sanctions efficaces en cas de non-respect, et ne requièrent pas la mise en oeuvre de procédures de diligence raisonnable. Il a été néanmoins mis en lumière que les obligations de reporting qui sont, pour la plupart, relativement récentes, ont eu un impact positif en ce qu'elles ont permis une sensibilisation accrue aux incidences négatives sur certains sujets particuliers.

La majorité des parties prenantes ont indiqué que l'introduction au niveau européen d'un devoir légal de diligence des entreprises en tant que norme de conduite (Option 4) serait de nature à fournir des avantages potentiels pour les entreprises en termes d'harmonisation, de sécurité juridique, de règles du jeu équitables, et de pouvoir d'influence accru sur leurs relations commerciales au sein de leurs chaînes d'approvisionnement par le biais de l'introduction de normes non-négociables. Les règles du jeu équitables et la sécurité juridique font partie des motivations les plus importantes pour les personnes interrogées parmi les entreprises, tandis que les personnes interrogées parmi les autres parties prenantes ont mis en exergue le potentiel d'une telle option dans le cadre de l'amélioration de l'accès aux recours pour les personnes affectées, et l'amélioration de la mise en œuvre des obligations de diligence raisonnable. La quasi-totalité des personnes interrogées s'est montrée favorable à un changement réglementaire visant à introduire un devoir de diligence des entreprises au niveau européen, quand bien même leurs points de vue ont pu diverger sur les aspects concernant la responsabilité juridique des entreprises en cas de dommage et les mécanismes de mise en œuvre. A l'inverse, les répondants à l'enquête générale issus d'organisations industrielles ne se sont généralement pas montrés favorables à un changement réglementaire, et notamment à l'introduction d'un devoir de diligence contraignant.

Dans le cadre de cette dernière option, la préférence générale se dessine en faveur d'une réglementation transsectorielle qui prendrait néanmoins en compte les spécificités du secteur et la taille de la société dans le cadre de sa mise en oeuvre. Les répondants à l'enquête ont fait part de leur préférence générale pour une norme susceptible de s'appliquer à l'ensemble des entreprises, quelle que soit la taille, bien que les opinions varient à ce sujet: un certain nombre de personnes ont indiqué leur préoccupation quant à la charge potentielle d'une telle réglementation pour les petites et moyennes entreprises (PME), tandis que d'autres ont fait valoir que de nombreux risques afférents à leur chaîne d'approvisionnement sont liés aux activités des PME.

Les parties prenantes ont en outre indiqué que le devoir de diligence doit faire référence à une norme de conduite et non à une exigence procédurale (souvent décrite comme un exercice de « cochage des cases») et elles ont indiqué qu'une entreprise devrait pouvoir s'exonérer de sa responsabilité juridique en démontrant avoir mis en oeuvre la diligence raisonnable requise aux vues des circonstances (défense de diligence raisonnable). Les personnes interrogées ont également souligné que toute loi relative au devoir de diligence devrait faire partie d'un « assortiment judicieux » de mesures. Certaines parties prenantes ont remarqué qu'une période de transition serait utile. D'autres ont indiqué qu'une réglementation au niveau européen liée à des exigences juridiques en termes d'opérations sur le marché européen, ou d'accès au marché européen pourrait constituer une puissante incitation au respect de la règlementation. De nombreuses parties prenantes ont souligné l'importance globale du leadership de l'UE dans ce domaine.

On soulignera que, individuellement, les entreprises multinationales sont de plus en plus nombreuses à soutenir l'introduction d'un devoir de diligence, même si des divergences d'opinions se font jour en ce qui concerne le régime de sanction pouvant l'accompagner. A l'inverse, la majorité des répondants à l'enquête générale issus d'organisations industrielles ont indiqué une préférence pour les options réglementaires les moins contraignantes. À cet égard, les points de vue des organisations industrielles sur les options réglementaires contredisent donc fréquemment celles des entreprises multinationales prises individuellement.

Un consensus de l'ensemble des parties prenantes semble se dégager (avec un grand nombre d'opinions particulièrement énergiques sur ce point), quant au fait que le concept de diligence raisonnable des principes directeurs des Nations Unies ne devrait pas être abandonné au profit d'un autre concept plus « vague ». Les parties prenantes ont suggéré que tout nouveau mécanisme réglementaire au niveau européen devrait s'appuyer sur le concept de diligence raisonnable des principes directeurs des Nations-Unies afin de tirer parti de leur influence considérable.

3. Étude réglementaire (Tâche 2)

Cette partie de l'étude a passé en revue le cadre normatif ayant trait à la diligence raisonnable en matière de droits de l'homme et de protection de l'environnement à laquelle sont tenues les entreprises, à la fois au niveau européen et international ainsi qu'au niveau domestique, et plus particulièrement dans 12 Etats membres de l'UE analysés dans le cadre de rapports d'experts, ainsi que dans certains pays hors de l'UE.

Les Principes directeurs des Nations Unies prévoient que, pour s'acquitter de leur responsabilité en matière de respect des droits de l'homme, les entreprises doivent faire preuve de diligence raisonnable en matière de droits de l'homme[48] afin d'« identifier, de prévenir, d'atténuer et de rendre compte» des incidences potentielles ou effectives sur les droits de l'homme dans lesquelles elles peuvent avoir une part que ce soit par le biais

[48] Principes directeurs N°15 -21

de leurs propres activités, ou du fait de leurs relations commerciales.[49] Cette responsabilité qui incombe aux entreprises de respecter les droits de l'homme s'applique à toutes les entreprises, indépendamment de leur taille, de leur secteur ou du contexte local au sein duquel elles opèrent.[50] Les Principes directeurs des Nations Unies font référence à la chaîne de valeur (et non pas à la chaîne d'approvisionnement),[51] et étendent la responsabilité de l'entreprise aux incidences négatives sur les droits de l'homme que l'« entreprise *peut avoir ou auxquelles elle peut contribuer* par le biais de ses propres activités, ou qui peuvent *découler directement* de ses activités, produits ou services par ses relations commerciales ».[52] Le concept d'influence est utilisé afin de déterminer les "mesures nécessaires" qui doivent être prises par l'entreprise lorsqu'elle contribue à une incidence négative sur les droits de l'homme, ou que cette incidence est directement liée à son activité, ses produits ou ses services par sa relation commerciale avec une autre entité.[53] L'entreprise est considérée comme exerçant un tel pouvoir d'influence lorsqu'elle « a la capacité d'apporter des changements aux pratiques illicites d'une entité qui commet un abus».[54] Les Principes directeurs des Nations Unies indiquent que la diligence raisonnable en matière de droits de l'homme doit s'exercer en permanence (et ne pas être un événement exceptionnel), être adaptée au contexte spécifique de l'entreprise (et ne pas se réduire à un exercice uniformisé consistant à cocher des cases) et couvrir l'ensemble des droits de l'homme,[55] bien que certains domaines où le risque d'incidences négatives sur les droits de l'homme est le plus important puissent bénéficier d'un ordre de priorité pour l'exercice de la diligence raisonnable.[56] La diligence raisonnable en matière de droits de l'homme doit couvrir les risques encourus par les titulaires de droits (c'est à dire, les parties prenantes et la planète) et donc s'étendre au-delà des risques auxquels l'entreprise est elle-même exposée.[57]

L'influence considérable des Principes directeurs des Nations-Unies est manifeste aux vues de l'adoption répandue du concept de diligence raisonnable dans les normes internationales qui ont été adoptées par la suite. Par exemple, les Principes directeurs de l'OCDE ont été mis à jour en 2011 afin de s'aligner sur les Principes directeurs des Nations-Unies,[58] et le guide OCDE sur le devoir de diligence pour une conduite responsable des entreprises se fonde sur un standard de diligence raisonnable similaire à celui retenu par les Principes directeurs des Nations-Unies, et qui s'étend «à tous les niveaux de la chaîne d'approvisionnement ou de la chaîne de valeur de l'entreprise».[59] Les Principes directeurs de l'OCDE ont étendu le concept de diligence raisonnable à d'autres domaines tels que l'environnement et le changement climatique, l'emploi et les relations professionnelles, la lutte contre la corruption, la sollicitation de pots-de-vin et autres formes d'extorsion, et les intérêts des consommateurs.[60] Les gouvernements adhérents aux Principes directeurs de l'OCDE sont tenus de mettre en place des Points de contact nationaux (« PCNs ») chargés de répondre aux saisines pour non-respect des principes directeurs de l'OCDE.

L'UE a pris un certain nombre d'initiatives qui imposent certaines obligations de diligence raisonnable aux entreprises pour leurs impacts négatifs sur les droits de l'homme et l'environnement, y compris leurs impacts sur le climat. On peut citer à titre d'exemple de

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[49] Principe directeur N° 15
[50] Principes directeurs N° 14 et 23.
[51] Principe directeur N° 13 et son commentaire
[52] Principe directeur N° 17
[53] Principe directeur N° 17 et son commentaire.
[54] Commentaire du principe directeur 19
[55] John Ruggie, « Protéger, respecter et réparer: un cadre pour les entreprises et les droits de l'homme», 7 avril 2008, A/HRC/8/5 au paragraphe 8.
[56] Principe directeur N° 17 et son commentaire
[57] OCDE, *Principes directeurs de l'OCDE à l'intention des entreprises multinationales*, 2011.
[58] John Ruggie et Tamaryn Nelson, « Human RIghts and the OECD Guidelines for Multinational Enterprises: Normative Innovations and Implementation Challenge», Mai 2015, Corporate Social Responsibility Initiative Working Paper No. 66, p. 13.
[59] OCDE, *Principes directeurs de l'OCDE à l'intention des entreprises multinationales*, 2011, paragraphe 14.p. 40.
[60] OCDE, *Guide OCDE sur le devoir de diligence pour une conduite responsable des entreprises*, 2018, p. 68

règlementations sectorielles, le règlement établissant les obligations des opérateurs qui mettent du bois et des produits dérivés sur le marché (EUTR) [61] (qui est entré en vigueur préalablement à l'adoption des Principes directeurs des Nations-Unies), ainsi que le règlement relatif aux minerais provenant de zones de conflit,[62] qui entrera en vigueur le 1er janvier 2021. L'UE a également adopté la directive concernant la publication d'informations non financières,[63] ainsi que ses lignes directrices non contraignantes sur l'information non financière,[64] et son récent supplément relatif aux informations en rapport avec le climat.[65]

Diverses mesures législatives nationales comportent des obligations de diligence dans les chaînes d'approvisionnement, mais elles demeurent généralement spécifiques à un secteur ou à un sujet particulier. La loi française sur le devoir de vigilance de 2017[66] représente, à ce jour, le seul exemple législatif consacrant un devoir de diligence raisonnable général en matière de droits de l'homme et d'environnement. Cette loi étant relativement récente, elle n'a pas encore fait l'objet de jurisprudence de nature à apporter des précisions sur son interprétation et sur sa mise en oeuvre, néanmoins les premières actions en justice ont été engagées.[67] La loi britannique sur l'esclavage moderne de 2015[68] impose des obligations de transparence en matière d'esclavage moderne et de traite des êtres humains et la loi néerlandaise sur le devoir de diligence en matière de travail des enfants de 2019 impose des obligations de diligence raisonnable en matière de travail des enfants.[69] Des propositions de lois et des campagnes relatives à l'introduction de législations relatives au devoir de vigilance en matière de droits de l'homme et d'environnement sont actuellement en discussion au sein de 13 pays européens, dont 11 Etats-membres. D'autres législations nationales contiennent certaines exigences en matière de diligence raisonnable à l'instar des lois en matière de lutte contre la corruption, de sécurité des produits, de marchés publics, de lutte contre le blanchiment d'argent et de devoirs des administrateurs. Certaines obligations de diligence raisonnable dans la chaîne d'approvisionnement sont limitées à des secteurs spécifiques, tels que le secteur du bois, des minerais ou la sécurité alimentaire. Des obligations de diligences raisonnables sont également envisagées dans le Projet de Traité révisé de l'ONU sur les entreprises et les droits de l'homme.[70]

En l'absence de devoir de diligence raisonnable général en matière de droits de l'homme et d'environnement dans la plupart des pays européens, la jurisprudence des Etats membres a développé diverses pistes permettant de poursuivre des entreprises en justice pour leurs impacts négatifs sur les droits de l'homme ou sur l'environnement, notamment sur le plan de la responsabilité civile délictuelle, sur le plan pénal ou en termes de protection des consommateurs. Certaines actions en justice ont également été intentées à l'encontre d'entreprises en raison de leurs contributions au changement climatique.

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[61] Règlement (UE) No 995/2010 du Parlement européen et du conseil 20 octobre 2010 établissant les obligations des opérateurs qui mettent du bois et des produits dérivés sur le marché.

[62] Règlement (UE) 2017/821 du Parlement européen et du Conseil du 17 mai 2017 fixant les obligations liées au devoir de diligence à l'égard de la chaîne d'approvisionnement pour les importateurs de l'Union qui importent de l'étain, du tantale et du tungstène, leurs minerais et de l'or provenant de zones de conflit ou à haut risque

[63] Directive 2014/95/UE du Paiement européen et du Conseil du 22 octobre 2014, modifiant la directive 2013/34/UE en ce qui concerne la publication d'informations non financières et d'informations relatives à la diversité par certaines grandes entreprises et certains groupes.

[64] Commission Européenne, Lignes directrices sur l'information non financière (méthodologie pour la communication d'informations non financières) (2017/C 215/01).

[65] Commission Européenne, Lignes directrices sur l'information non financière: Supplément relatif aux informations en rapport avec le climat (2019/C 209/01).

[66] Loi no. 2017-399 du 27 Mars 2017 relative au devoir de vigilance des sociétés mères et des entreprises donneuses d'ordre

[67] Voir notamment Environment News Service (ENS) «Total Sued Under France's New Duty of Vigilance Law », 23 Octobre 2019, consultable à l'adresse suivante: http://ens-newswire.com/2019/10/23/total-sued-under-frances-new-duty-of-vigilance-law/

[68] UK Modern Slavery Act 2015, s 54. Voir l'étude règlementaire et le rapport de Pays concernant le Royaume-Uni.

[69] *Kamerstukken I*, 2016/17, 34 506, A. Voir l'étude règlementaire et le rapport de Pays concernant les Pays-Bas.

[70] OEIGWG, « Legally Binding Instrument to Regulate, in International Human Rights Law, the Activities of Transnational Corporations and Other Business Enterprises», 16 Juillet 2019.

Un certain nombre de développements très récents (en grande partie survenus au cours de la réalisation de cette étude) sont venus préciser la teneur des obligations de diligence raisonnable des entreprises concernant leurs impacts sur le changement climatique. En particulier, en avril 2019 le Point de contact national des Pays-Bas a éclairci pour la première fois les moyens concrets par le biais desquels les entreprises peuvent inclure dans leur mesures de diligence raisonnable leurs objectifs en termes de lutte contre le changement climatique, même en l'absence de mesures et de normes internationales contraignantes sur le sujet.[71] A cet effet, la décision du PCN fait référence à l'Accord de Paris sur le climat.[72]

4. Analyse des problèmes et Options réglementaires (Tâche 3)

Cette partie de l'étude a consisté en une analyse des problèmes, une logique d'intervention et l'identification des éventuelles options d'interventions réglementaires suivantes au niveau européen:[73]

Option 1: Aucun changement règlementaire (scénario de référence)

Cette option n'entraînerait aucune modification de la réglementation au niveau de L'UE en matière de devoir de diligence des entreprises tout au long de leurs chaînes d'approvisionnement. Il est cependant escompté que les développements législatifs au niveau national aboutiront à l'adoption de réglementations introduisant un devoir de diligence raisonnable dans un certain nombre d'Etats membres.

Option 2: Nouvelles lignes directrices/orientations volontaires

Cette option impliquerait de nouvelles lignes directrices volontaires au niveau européen en matière de devoir de diligence des entreprises dans leurs chaînes d'approvisionnement. Par définition, les lignes directrices volontaires ne sont pas juridiquement contraignantes mais pourraient avoir une influence sur les normes de conduites attendues des entreprises.

Option 3: Nouvelle réglementation imposant de obligations en matière de transparence (reporting)

Cette option entraînerait l'adoption d'une nouvelle réglementation au niveau européen qui imposerait aux entreprises des obligations de rendre compte des mesures qu'elles implémentent afin d'identifier, de prévenir et d'atténuer les incidences négatives effectives ou potentielles sur les droits de l'homme et sur l'environnement par le biais de leurs propres opérations et de leurs relations commerciales (y compris au sein de leurs chaînes d'approvisionnement ou de leurs chaînes de valeur).[74] Cette option pourrait se différencier des exigences découlant de la directive concernant la publication d'informations non financières en ce qui concerne le niveau de détail et de transparence requis, ainsi qu'une approche centrée sur les risques pour les détenteurs de droits et la planète, plutôt que sur les risques pour les actionnaires.

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[71] Voir la déclaration finale du point de contact national des Pays-Bas, consultable à l'adresse suivante: https://www.oecdguidelines.nl/documents/publication/2019/04/19/ncp-final-statement-4-ngos-vs-ing.

[72] Voir l'Accord de Paris sur le climat, consultable à l'adresse suivante: https://unfccc.int/fr/process-and-meetings/the-paris-agreement/l-accord-de-paris.

[73] D'autres considérations identifiées comme pertinentes dans le cadre la mise en œuvre d'une nouvelle intervention réglementaire sont abordée dans le rapport complet et comprennent l'éventuelle adoption de lignes directrices non contraignantes venant préciser le devoir de diligence, la réglementation des activités transnationales des entreprises, l'application aux groupes d'entreprise et la chaîne d'approvisionnement, la mise en œuvre au niveau des États membres, la portée matérielle relative à la définition des droits de l'homme et des impacts environnementaux, les aspects de conflit de lois, et la période de transition.

[74] Cela dépendra de la portée de l'intervention réglementaire. Le titre de l'étude et les termes de référence se réfèrent à la notion de chaîne d'approvisionnement, mais la portée du mandat qui est décrit envisage une application du devoir de diligence qui s'étende à l'ensemble de la chaîne de valeur. Des définitions ont été fournies aux répondants au sondage lorsqu'ils ont été interrogés relativement à leurs « chaînes d'approvisionnement an amount » et à leurs « chaînes de valeur en aval».

Option 4: Nouvelle réglementation introduisant un devoir de diligence

Cette option impliquerait l'introduction, au niveau européen, d'un devoir de diligence qui imposerait aux entreprises de mettre en place des mesures de diligence raisonnable propres à identifier, prévenir, atténuer et rendre compte des impacts négatifs, potentiels ou effectifs, sur les droits de l'homme et l'environnement résultant de leurs propres activités et de leurs chaînes d'approvisionnement ou de leurs chaînes de valeur.[75] Une entreprise pourrait démontrer, en tant que défense, qu'elle a respecté cette norme en mettant en oeuvre le *niveau requis de diligence raisonnable en tenant compte des circonstances particulières*. Il s'agirait d'une approche basée sur les risques et le contexte particulier au sein duquel l'entreprise opère. L'exercice de la diligence raisonnable permettrait l'établissement d'un ordre de priorité de ces risques, en fonction de leur «gravité »[76] de leur caractère « significatif »[77] ou des sujets les plus « saillants ».[78]

Sous-catégorie 4.1 : Nouvelle réglementation relative à une catégorie étroite d'activités (limitées par secteur)

Dans le cadre de cette sous-catégorie, le devoir de diligence serait limité à certains secteurs particuliers, à certaines marchandises particulières ou à certains risques particuliers (travail des enfants).

Sous-catégorie 4.2 : Nouvelle réglementation applicable horizontalement à tous les secteurs

Cette sous-catégorie prévoit que le devoir de diligence mentionné ci-dessus (Option 4) s'appliquerait à tous les secteurs, soit (a) à un ensemble défini de grandes entreprises; (b) soit à l'ensemble des entreprises quelle que soit leur taille et y compris les PME ; soit (c) qu'il pourrait y avoir une obligation générale pour toutes les entreprises à laquelle viendrait s'ajouter une obligation supplémentaire uniquement pour les grandes entreprises.

Sous-catégorie 4.2(a) : application limitée à un ensemble défini de larges entreprises

Cette sous-catégorie entraînerait un devoir général de diligence (Option 4) applicable à un ensemble défini de grandes entreprises.

Sous-catégorie 4.2(b) : application à toutes les entreprises, y compris les PME

Cette sous-catégorie entraînerait un devoir général de diligence (option 4) applicable à l'ensemble des entreprises, y compris les PME.

Option subsidiaire 4.2(c) : devoir général pour toutes les entreprises plus des obligations supplémentaires spécifiques aux grandes entreprises

Cette sous-catégorie impliquerait l'adoption d'un devoir général de diligence raisonnable pour l'ensemble des entreprises, y compris les PME, auquel viendrait s'ajouter une obligation spécifique aux grandes entreprises. Cela pourrait par exemple consister en un devoir général s'appliquant à l'ensemble des entreprises, auquel viendrait s'ajouter une

[75] Ibid.
[76] Principe directeur N° 17(b).
[77] Lignes directrices de l'OCDE sur les entreprises multinationales, chapitre II, Commentaire, paragraphe 16.
[78] Shift and Mazars, Cadre de reporting conforme aux principes directeurs des Nations-Unies, avec guide de mise en œuvre, consultable à l'adresse suivante : https://www.ungpreporting.org/wp-content/uploads/2017/05/UNGPReportingFramework_wguidance-FR.pdf, p. 22.

obligation supplémentaire uniquement pour les grandes entreprises en termes d'objectifs de lutte contre le changement climatique alignés sur les objectifs de l'Accord de Paris sur le climat.

Sous-catégorie 4.3 : Les sous-catégories 4.1 et 4.2 accompagnées par un mécanisme de supervision et/ou un mécanisme d'exécution.

Afin de garantir sa mise en œuvre effective, la nouvelle réglementation introduisant un devoir de diligence raisonnable (Option 4) devrait être accompagnée d'un mécanisme de surveillance et/ou d'un mécanisme d'exécution. Cette sous-catégorie est divisée en deux sous-catégories concernant le régime de supervision et de sanctions en cas de non-respect, à savoir (a) par le biais de recours judiciaires et non judiciaires, ou (b) par le biais d'un organisme de supervision étatique apte à imposer des sanctions en cas de non-respect. Ces deux sous-catégories ne s'excluent pas mutuellement et pourraient toutes les deux être applicables au sein du même instrument.

Sous-catégorie 4.3(a) : mécanismes pour les recours judiciaires et non judiciaires

Cette sous-catégorie consisterait en l'introduction du devoir de diligence mentionné ci-dessus (option 4) accompagnée de mécanismes de recours judiciaires et non judiciaires pour les personnes affectées par l'échec de mise en oeuvre du devoir de diligence.

Sous-catégorie 4.3(b) : organisme de supervision public et régime de sanctions en cas de non-conformité

Cette sous-catégorie consiste à introduire un devoir de diligence mentionné ci-dessus (Option 4) accompagné d'un organisme de supervision public pouvant imposer des sanctions en cas de non-respect. Les autorités de supervision et d'exécution (souvent appelés organismes administratifs) pourraient être mis en place au niveau de l'UE et/ou des États membres, au sein des services publics existants, ou dans le cadre d'organismes nouveaux. Le régime de sanctions dont ils disposent pourrait inclure des amendes, la désignation de systèmes de surveillance, le retrait de licences ou de concessions commerciales ou même la dissolution de la société. Cependant, il convient de noter qu'aucun de ces mécanismes ne comprend de recours pour les victimes, ce qui constitue une limitation, même s'il n'est pas exclu qu'une telle option de recours puisse être expressément prévue en plus du mécanisme de supervision public.

5. Analyse des options

L'analyse économique des options réglementaires a été entreprise par LSE Consulting sur la base d'un examen de la littérature et d'une évaluation des résultats de l'enquête. Elle associe des approches quantitatives et qualitatives et vise à présenter et à évaluer, de manière préliminaire,[79] les coûts et les avantages possibles des différentes options réglementaires dans les domaines suivants: impacts économiques, impacts sociaux, impacts environnementaux, impacts sur les droits de l'homme, et impacts pour les autorités publiques au sein de l'UE.[80] Il est important de souligner que les différentes parties prenantes ont été exposées à des expériences différentes de lois en matière de diligence raisonnable, de reporting et d'exigences administratives. L'absence d'exemples

[79] L'analyse d'impact dont il s'agit ici est une analyse préliminaire des options réglementaires, et non pas une étude d'impact exhaustive accompagnant une proposition de réglementation. En tant que telle, l'analyse d'impact doit être considérée comme une discussion générale des impacts potentiels qui pourraient survenir dans l'hypothèse et au moment où une nouvelle régulation serait élaborée.
[80] Compte tenu du caractère récent des lois introduisant un devoir de diligence, il s'est avéré difficile de trouver des analyses d'impacts des lois en questions, et celles qui ont été trouvées, ne contenaient pas nécessairement des informations et/ou des données pouvant servir à notre analyse.

de législations similaires sur le plan comparé a entraîné des attentes diverses parmi les répondants à l'enquête.

La quantification des impacts économiques pour les entreprises repose sur des estimations de jours-personnes qui ont été fournies par les répondants à l'enquête parmi les entreprises pour chacune des quatre options règlementaires. De manière générale, les estimations des entreprises indiquent que le nombre de jours-personnes nécessaires et les coûts afférents, augmenteraient modérément en cas de changement réglementaire allant du « statu quo » à de « nouvelles obligations en matière de transparence (reporting) » et augmenteraient sensiblement en cas de changement allant du « statu quo » à « l'introduction d'un devoir de diligence ». Nous estimons que l'impact total sur les coûts annuels supplémentaires propres aux entreprises des 28 Etats membres de l'UE (frais de main-d'œuvre, frais généraux, et coûts des activités externalisées) serait proportionnellement plus élevé en ce qui concerne l'Option 4, avec des variations à prévoir en fonction de la taille et du secteur de l'entreprise, ainsi qu'en fonction du champ d'application de l'option réglementaire.

L'impact pour la concurrence et l'innovation est difficile à évaluer ex-ante. De manière générale, aucune distorsion significative de la concurrence intra-UE n'est attendue si toutes les entreprises opérant au sein l'UE sont soumises au même ensemble de réglementations. S'il est possique que les entreprises européennes subissent un désavantage concurrentiel relatif par rapport aux entreprises non-européennes, les coûts supplémentaires considérés en tant que pourcentage des revenus seront relativement faibles comparativement, par exemple, au tarif standard appliqué aux marchandises importées dans l'UE. Par conséquent, aucune distorsion significative pour les exportateurs de l'UE résultant d'une augmentation des coûts administratifs récurrents n'est escomptée. Les répondants à l'enquête destinée aux entreprises estiment qu'ils bénéficieraient d'avantages significatifs, voire même très significatifs, grâce à la réduction des distorsions, si la nouvelle réglementation européenne créait des normes plus égalitaires pour les fournisseurs européens et non-européens.

Par ailleurs, les parties prenantes ont indiqué rencontrer un certain nombre de difficultés en raison du manque de réglementation actuel caractérisant le statu quo, et qu'ils escompteraient une amélioration si un devoir général de diligence était introduit au niveau européen. Les avantages qui résulteraient d'une telle option réglementaire incluent en particulier une amélioration de la compétitivité au travers du nivellement des règles du jeu, qui impliquerait que les concurrents, les pairs, les fournisseurs et les tiers seraient soumis aux mêmes standards, ainsi qu'une augmentation du pouvoir d'influence des entreprises sur leurs relations commerciales au sein de leurs chaînes de valeur par le biais de l'introduction de normes non-négociables. Ces avantages, qui sont difficiles à quantifier à ce stade, doivent néanmoins être gardés à l'esprit en ce qu'ils pourraient se révéler significatifs et ont été évoqués par les parties prenantes issues des entreprises parmi les raisons les plus importantes au soutien de l'introduction d'un devoir de diligence des entreprises.

De manière similaire, les répondants à l'enquête destinée aux entreprises ont fait valoir que les risques réputationnels figuraient parmi les incitations principales à la mise en oeuvre de mesures de diligence raisonnable dans le cadre du statu quo actuel. Il est escompté que l'introduction d'un devoir de diligence réduirait les risques réputationnels et qu'il s'agirait d'un des avantages les plus significatifs.

L'étude note que la numérisation et les outils des nouvelles technologies ont le potentiel de fournir des solutions sans précédent permettant d'identifier, de remédier et d'éliminer les violations des droits de l'homme et de l'environnement. Cependant, ces avancées technologiques n'ont pas été prises en considération par la vaste majorité des répondants.

Les impacts liés aux coûts pour les autorités publiques des Options 2 et 3 devraient rester limités. Les coûts supplémentaires pour la supervision de la mise en œuvre de la réglementation au titre de l'Option 4 seraient plus significatifs, en particulier dans l'hypothèse où un mécanisme public d'exécution était mis en place par les Etats membres ou au niveau européen (sous-catégorie 4.3). En comparaison, les recours judiciaires prévus à la sous-catégorie 4.3(a) pourraient entraîner des coûts largement inférieurs pour les États membres puisque ces coûts seraient inclus dans les budgets existants pour les tribunaux et le système judiciaire.

Les Options 2 et 3 ne devraient avoir qu'un impact social positif mineur. Dans la mesure où ces options se bornent à fournit de nouvelles lignes directrices ou à imposer des obligations en matière de transparence (reporting), sans toutefois imposer aux entreprises de mettre en oeuvre de manière substantielle des mesures de diligence raisonnable, il n'est pas escompté que les entreprises mettent en place des mesures supplémentaires substantielles afin d'aborder les enjeux sociaux. Il n'est pas non plus attendu que l'une ou l'autre des options ait d'impacts majeurs, positifs ou négatifs, sur les niveaux d'emploi. Il est escompté que les impacts sociaux de l'Option 4 seraient les plus significatifs puisque l'option réglementaire en question imposerait des obligations de mise en oeuvre de pratiques de diligence raisonnable. Toutefois, l'ampleur et le type des impacts sociaux dépendra de la conception de la nouvelle régulation et de sa mise en oeuvre, des enjeux sociaux dont la régulation traite, ainsi que de l'efficacité des mécanismes de mise en oeuvre. De manière similaire, les impacts sur les droits de l'homme et l'environnement de l'Option 4 sont considérés comme étant les plus significatifs, bien que l'ampleur exacte de ces impacts positifs dépendent de la supervision et de l'exécution de la règlementation. Si l'on compare les Options 2 et 3, les répondants considèrent que les lignes directrices volontaires seraient plus efficaces que des exigences de reporting en termes d'impacts positifs. Les impacts positifs attendus sont conformes aux analyses d'impacts antérieures de l'UE.

I. INTRODUCTION

1. Introduction

This is the final report delivered for the European Commission for JUST/2018/COMM/FW/RIGH/0070 (2018/03) on a study on due diligence through the supply chain. For this study, the British Institute of International and Comparative Law (BIICL) leads a research consortium in partnership with Civic Consulting and LSE Consulting.

This report is based on the methodology set out in the Technical Annex to the request for service under Framework contract n° JUST/2015/PR/01/0003 ("the offer"), which corresponded to the request for services or terms of reference (hereafter "TOR").

The report is structured around the following main parts:[81]

- Introduction
- Market practices (Task 1)
- Regulatory review (Task 2)
- Problem analysis and regulatory options (Task 3)
- Assessment of regulatory options (Task 4)

2. Background

Action 10 of the European Commission Action Plan on Financing Sustainable Growth of 8 March 2018 provides a mandate to:[82]

> [C]arry out analytical and consultative work with relevant stakeholders to assess: (i) the possible need to require corporate boards to develop and disclose a sustainability strategy, including *appropriate due diligence throughout the supply chain*, and measurable sustainability targets; and (ii) the possible need to clarify the rules according to which directors are expected to act in the company's long-term interest. [Our emphasis].

In its May 2018 Report on Sustainable Finance, the European Parliament "[c]alls on the Commission" to provide a "legislative proposal…" for:[83]

> [A]n *overarching, mandatory due diligence framework including a duty of care* to be fully phased-in within a transitional period and taking into account the proportionality principle. [Our emphasis]

The European Parliament report further:[84]

> [C]alls also for a proportionate *mandatory due diligence framework* based on the 2017 OECD Guidelines for Responsible Business Conduct for Institutional Investors, requiring investors to *identify, prevent, mitigate and account* for ESG factors after a transitional period; upholds that this pan-European framework should be based on the *French Corporate Duty of Vigilance Law* for companies and investors, including banks...

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[81] Technical Annex to the request for service under Framework contract n° JUST/2015/PR/01/0003 ("TOR") at 17.
[82] Action 10 of the Communication from the Commission to the European Parliament, the European Council, the Council, the European Central Bank, the European Economic and Social Committee and the Committee of the Regions Action Plan: Financing Sustainable Growth, COM/2018/097 final, 8 March 2018, available at: https://ec.europa.eu/info/publications/180308-action-plan-sustainable-growth_en.
[83] European Parliament Report on Sustainable Finance, (2018/2007(INI)), 4 May 2018, available at: http://www.europarl.europa.eu/doceo/document/A-8-2018-0164_EN.html at para 6.
[84] Ibid at para 11.

These two documents – hereafter referred to as "the Action plan" and "the European Parliament report" respectively - and in particular the above-mentioned references to *mandatory due diligence*,[85] form the background for the mandate for this study.

As stated in the European Parliament report, and elaborated on in the TOR, the concept of due diligence relevant to this study is due diligence to "identify, prevent, mitigate and account for" adverse corporate impacts, which is the language introduced by the UN Guiding Principles on Business and Human Rights ("UNGPs"),[86] and incorporated into the OECD Guidelines for Multinational Enterprises ("OECD Guidelines")[87] to extend to other areas of responsible business conduct such as the environment and climate change, conflict, labour rights, bribery and corruption, disclosure and consumer interests,[88] as well as into the ILO Tripartite declaration of principles concerning multinational enterprises and social policy ("MNE Declaration").[89] It is also the foundation for the French Duty of Vigilance Law, which requires due diligence (*vigilance*) for human rights and environmental harms,[90] and which the European Parliament report states should be the *basis for the "pan-European framework"*.[91]

In describing the context for this study, the TOR further elaborates on the background to this study as follows:[92]

> [D]espite recent developments in many EU companies, many argue that regulatory changes are necessary to foster and underpin the transition to more sustainable business models.
>
> A number of recent international developments point to the need for the legislator to establish a legal framework requiring business entities to exercise human rights due diligence in order to identify, prevent and mitigate the risks of violations of relevant rights. However, the objective of respecting people when it comes to the boundaries of economic value creation and business activities are only one side of the sustainability agenda. Other so-called planetary boundaries include the environment and climate change.
> At the EU level sectorial mandatory human rights [and environmental] due diligence obligations had been established for certain economic operators, like

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[85] Both the Action Plan and the Initiative Report contain multiple other actions which are relevant to sustainability. These are related, and may be referred to on occasion in this report, but are not the focus of this study in terms of the technical details set out in the TOR.
[86] UN Office of the High Commissioner for Human Rights ("OHCHR") "Guiding Principles on Business and Human Rights: Implementing the 'Protect, Respect and Remedy' Framework", HR/PUB/11/04, 2011 ("UNGPs"), available at: https://www.ohchr.org/documents/publications/GuidingprinciplesBusinesshr_eN.pdf.
[87] OECD Guidelines for Multinational Enterprises 2011, available at: https://www.oecd.org/corporate/mne/. See also the OECD "OECD Guidelines for Multinational Enterprises: Responsible Business Conduct Matters" ("OECD RBC Guidance"), available at: http://mneguidelines.oecd.org/MNEguidelines_RBCmatters.pdf; and the 2017 OECD Guidelines for Responsible Business Conduct for Institutional Investors, available at: https://mneguidelines.oecd.org/RBC-for-Institutional-Investors.pdf and mentioned in para 11 of the European Parliament report above n 84.
[88] OECD Guidelines ibid Commentary on General Policies at para 14.
[89] ILO, Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy, adopted by the Governing Body of the International Labour Office at its 204th Session (Geneva, November 1977) and amended at is 279th (November 2000), 295th (March 2006) and 329th (March 2017) Sessions ("ILO MNE Declaration").
[90] Sherpa, "Vigilance Plans Reference Guidance", 1st ed., 2018, available at: https://www.asso-sherpa.org/wp-content/uploads/2019/02/Sherpa_VPRG_EN_WEB-VF-compressed.pdf at 11.
[91] The TOR at 3 provides that "[t]his exercise [i.e. this study] is meant to provide the Commission with elements for this assessment."
[92] The TOR continues to elaborate in more detail on the developments in due diligence which are relevant to this study, starting with the UNGPs, and followed by: recent interpretations by UN bodies relating to the human rights treaty obligations of states to "adopt a legal framework requiring business entities to exercise human rights due diligence in order to identify, prevent and mitigate the risks of violations of relevant rights" (TOR at 5 and fn 6); the Council of Europe Recommendation on Business and Human Rights (Rec (2016)3; TOR at 6); the OECD Guidelines for Institutional Investors above n 87; TOR at 6); and extraterritoriality in international human rights treaties (TOR at 6). The TOR thereafter discusses in more detail: "Calls for a mandatory Human Rights due diligence in Europe" (TOR at 6); EU competence on human rights (TOR at 7-8.); due diligence obligations in EU (sectoral) policy instruments (TOR at 8); and National laws on due diligence in Europe (TOR at 8-9). Some of the legal proposals discussed under this heading have since been adopted into law or developed further, and are discussed in the Regulatory Review section.

importers of conflict minerals [and timber products] for example, whereas the Non-Financial Reporting Directive introduced the concept of due diligence for a wider range of issues but it does not establish a mandatory duty for carrying out such procedures. While transparency requirements can be a way to incentivise companies not to do harm, embedding sustainability matters into corporate directors' duty of care through the establishment of due diligence procedures is considered by many to be more effective way to enhance responsible corporate behaviour.

These developments form the context of this study, and are discussed in further detail in the various sections of this report.

3. Scope and definitions

3.1 Scope

The aim of the study is:[93]

- to provide a detailed examination of the existing regulation and proposals for due diligence in companies' own operations and through the supply chain for adverse human rights and environmental impacts, including relating to climate change;

- to develop and assess regulatory options[94] for introducing due diligence requirements as a legal duty of care, including the initial perceptions of stakeholders relating to possible regulatory options.

For this purpose, and in accordance with the TOR, this report:

- analyses how companies define and implement due diligence processes to prevent, mitigate and account for adverse human rights and environmental impacts, including with respect to climate change;[95]

- focuses this analysis on processes and mechanisms to prevent abuses resulting from companies' own operations as well as in their supply and value chains.[96]

- maps and assesses existing and planned regulation or relevant industry codes, including relating to relevant perceptions relating to their use and impacts, as well as present and analyse evidence regarding "which measures are most efficient to ensure that companies effectively prevent such abuses and damage including in their supply chain and are held accountable in case such abuses or damage occur".[97]

- In accordance with the Better Regulation guidelines and toolbox: identifies the problems and their drivers; specifies under what intervention logic an EU initiative might possibly be launched to address these problems; identify the legal basis for the EU initiative; identifies possible options for introducing at EU level

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[93] TOR at 9.
[94] The study is aimed at identifying possible options for intervention at EU level. Indirectly, the scope of the study is global, insofar as the relevant stakeholders (multinational companies and rights-holders) may be operating in or affected by both EU and non-EU jurisdictions, through their own operations and supply chains.
[95] Specified in the TOR as "including the rights of the child and fundamental freedoms, serious bodily injury or health risks, environmental damage, including with respect to climate". The TOR further specifies at 9 that: "As regards the rights of the child and to child labour in the supply chains, the analysis should particularly focus on agriculture, including the coffee, tea and cocoa sectors."
[96] Described in the TOR as resulting "directly or indirectly from the operations of the company and of the companies it controls, as well as from the operations of the subcontractors or suppliers with whom it maintains a regular or an established commercial relationship". TOR at 9-10.
[97] TOR at 10.

requirements for companies to develop such processes; and assess the impacts of these options.[98]

It is noted that this this is an initial study for the development of regulatory options.

As such, it is not a public consultation on a regulatory proposal, and it is not a full-scale impact assessment which would accompany any such regulatory proposal.[99]

It is also noted that this study is not a review of the level of implementation of, or a fitness check of any existing regulatory measures, including the EU Non-Financial Reporting Directive, or of the uptake or implementation of the UNGPs. It is furthermore not itself a due diligence or impact assessment of corporate practices. The background to and mandate for this study is set out in detail above.

3.2 Definitions

The definitions for the purposes of this study are as follows. Where relevant, definitions were described to survey participants as part of the survey.

Based on this framework as set out in the TOR,[100] we will use the following definitions:

- **"Companies"** will be used to refer to all business enterprises, regardless of their legal format or structure of incorporation.

- **"Due diligence"** will be used in accordance with the definition used in the EU Parliament Report,[101] which is based on the description of due diligence introduced by the UNGPs (defined above). The UNGPs was a result of extensive stakeholder consultation by the Special Representative on Business and Human Rights, John Ruggie,[102] and was adopted unanimously by the UN Human Rights Council in 2011. While it is not a legally binding instrument, it is widely influential and constitutes the first authoritative global standard on business and human rights. This concept of due diligence has been introduced in various international instruments and standards, including the ILO's Tripartite declaration of principles concerning multinational enterprises and social policy (MNE Declaration) revised in 2017, the ISO's 26000 Social Responsibility Guidance Standard, and the UN Global Compact.[103] In particular, the OECD Guidelines were revised in 2011 to align with the UNGPs and the due diligence approach was not only applied to the human rights chapter, but also extended to other areas of responsible business conduct such as employment and industrial relations, environment and bribery.[104] Due diligence has also been referenced in a number of other EU and domestic regulatory instruments[105] including current legal developments for mandatory due diligence discussed in the TOR and described in further detail in the regulatory review section below.[106] The stakeholder views collected through the surveys and interviews (see section on market practices below) further confirm that the

[98] TOR at 10.
[99] The original timeline set for this study in the TOR was seven months.
[100] TOR at 4-9.
[101] Ibid.
[102] John Ruggie, *Just Business*, Norton, NY (2013) at 141-148.
[103] UN Global Compact, "Human Rights", available at: https://www.unglobalcompact.org/what-is-gc/our-work/social/human-rights.
[104] See, for example, the OECD Guidelines above n 87 and the Equator Principles, available at: https://equator-principles.com/.
[105] Chiara Macchi and Claire Bright, "Hardening Soft Law: The Implementation of Human Rights Due Diligence Requirements in Domestic Legislation", in M. Buscemi, N. Lazzerini and L. Magi, *Legal Sources in Business and Human Rights - Evolving Dynamics in International and European Law* (forthcoming, Brill, 2019).
[106] TOR 8-9.

concept of due diligence as introduced by the UNGPs provide the relevant framework for the discussion about due diligence for the purposes of this study.

- **"Due diligence through the supply chain or value chain"** for the purpose of this study, refers to due diligence processes to prevent, mitigate and account for human rights (including labour rights and working conditions) and environmental impacts, including relating to climate change, both in own operations and the supply chain. The study further looks at the current practices for downstream and value chain due diligence. "Supply chain" and "value chain", respectively, will be understood within the broad definition of a company's "business relationships" as described in the UNGPs,[107] and the OECD Guidelines. The title of the study in the TOR refers to the "supply chain", but the scope described in the TOR envisions a possible application of regulatory intervention to the entire value chain. Survey respondents were asked about current practices for due diligence both upstream and downstream in the value chain, and where relevant, detailed definitions relating to these respective concepts were provided to survey respondents.[108]

- **"Governance"** or **"corporate governance"** will be understood to include due diligence as part of corporate risk management and compliance.[109] Where relevant, country reports refer to the regulatory landscape for corporate governance areas such as anti-corruption, bribery and money-laundering, including how due diligence is used as a legal standard of care in these regulatory models, and how liability is applied in the context of parent companies, subsidiaries and suppliers. Anti-corruption models for due diligence inform the comparative analysis relating to the assessment of sub-options relating to enforcement and sanction.

- **"Human rights"** will be used to include all internationally and EU-recognised human rights, in line with the Charter of Fundamental Rights of the European Union. Human rights accordingly include, *inter alia*, all the rights contained in the Universal Declaration of Human Rights, the International Covenant on Civil and Political Rights and the International Covenant on Economic, Social and Cultural Rights, the principles concerning fundamental rights in the eight ILO core conventions, the Declaration on Fundamental Principles and Rights at Work, the ILO's Tripartite declaration of principles concerning multinational enterprises and social policy (MNE Declaration), the ILO Centenary Declaration for the Future of Work, the UN Convention of the Rights of the Child, the European Convention on Human Rights, the European Charter of Fundamental Rights, and rights set out in the main global human rights treaties and under customary international law.[110] For clarity, the study refers to "human rights and environmental" due diligence unless otherwise specified.

- **"Sustainability impacts"** will be understood within its meaning set out in the Better Regulation Guidelines and Toolbox to include social, environmental and

[107] The definition set out the Commentary to Guiding Principle 13 includes "relationships with business partners, entities in its value chain, and any other non-State or State entity directly linked to its business operations, products or services to include wider meaning of a company's business relationships". It is also noted that the Commentary to Guiding Principle 17 elaborates on the level of due diligence required through the supply chain and value chain: "Where business enterprises have large numbers of entities in their value chains it may be unreasonably difficult to conduct due diligence for adverse human rights impacts across them all. If so, business enterprises should identify general areas where the risk of adverse human rights impacts is most significant, whether due to certain suppliers' or clients' operating context, the particular operations, products or services involved, or other relevant considerations, and prioritize these for human rights due diligence"

108 For further information on the questions asked in the survey, please see Part II: Survey Results Statistics.

[109] See, for example, the following definition of corporate governance as set out in the Green Paper on Corporate Governance Institutions and Remuneration Policies, COM(2010) 284 final: "The traditional definition of corporate governance refers to relations between a company's senior management, its board of directors, its shareholders and other stakeholders, such as employees and their representatives. It also determines the structure used to define a company's objectives, as well as the means of achieving them and of monitoring the results obtained".

[110] TOR at 9.

human rights impacts. The surveys and assessment of the regulatory options are structured around an inclusive understanding of human rights and sustainability, and cover the following sustainability impacts, amongst others: air pollution (emissions of greenhouse gases, of carbon dioxide (CO_2), of sulphur oxides (SO_x), of nitrogen oxides (NO_x), and of particulates), waste, energy use and mix, water resources, biodiversity (including wildlife), rights of the child, right to life, liberty and security of person (including in this context, impacts on serious bodily injury), and right to the enjoyment of the highest attainable standard of physical and mental health (including, in this context, health risks impacts of business).[111] Stakeholders were also asked about the application of due diligence practices to large-scale negative economic impacts, such as profit-shifting to low tax jurisdiction.[112] The Regulatory Review discusses how due diligence fits in with the Sustainable Development Goals ("SDGs"), and more broadly with the sustainability framework.

4 Methodology

The detailed methodology for each task (evidence of market practices, the regulatory review and the assessment of regulatory options) is discussed in each respective section below.

In summary:

- The methodology for the collection of evidence on Market Practices (Task 1) consisted of surveys, interviews, case studies, and desktop and legal research of relevant materials. Interviews were undertaken by BIICL and Civic.

- The methodology for the Regulatory Review (Task 2) consisted of the collection of twelve Country Reports from legal experts with knowledge of due diligence in the relevant jurisdiction. Country Reports are contained in the annexure Part III Country Reports, and summarised and analysed in the Regulatory Review section. This summary is preceded by an overview of the nature of due diligence, based on a review of the relevant instruments, documents and literature.

- The methodology for the Problem Analysis and Regulatory Options (Task 3) consisted of an analysis of the problems and possible intervention options, based on the empirical evidence gathered in the section on market practices, as well as information about the regulatory framework set out in the regulatory review. The problem analysis and regulatory options were developed by BIICL and Civic Consulting.

- The section on the Assessment of regulatory options (Task 4) assesses the possible quantitative and qualitative impacts of the regulatory options developed. The Assessment of regulatory options was undertaken by LSE Consulting.

5 General Overview

Since this study was commissioned, the relevant landscape has changed significantly. The Netherlands have introduced a Child Labour Due Diligence Law.[113] Finland committed to undertake a study on a mandatory human rights due diligence law in

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[111] See the discussion in Karin Buhmann, Jonas Jonsson, Mette Fisker, "'Do no harm' and 'do more good' too: connecting the SDGs with business and human rights and political CSR theory", *Corporate Governance: The International Journal of Business in Society* (2018).

[112] Companies' tax saving behaviour is addressed through tax policy at national level and in international tax treaties, which exceed the scope of this project. Similarly, income inequality is driven by a myriad of factors such as taxation, social insurance, competition, and law-induced rents in various sectors of the economy, all of which exceed the scope of this analysis.

[113] *Kamerstukken I*, 2016/17, 34 506, A. See the Netherlands Country report.

Finland, and explore options for such a law at EU level.[114] In Italy, an open letter signed by over 50 academics and experts was addressed to the Italian institutions on 11 November 2019, stating that "the time is ripe for Italy to start a policy process towards the adoption of effective legislation on human rights due diligence, in line with its international obligations and with the positive example of other European countries."[115] In Germany, a draft outline for a suggested mandatory human rights and environmental due diligence law has been discussed amongst stakeholders, although it is not a formal draft proposal.[116]

Across Europe, various new campaigns have been launched for the introduction of domestic laws requiring mandatory due diligence for human rights and environmental impacts. During the course of this study, in May 2019, the Business and Human Rights Resource Centre launched a portal dedicated to tracking initiatives towards mandatory due diligence laws.[117] The portal currently lists 13 countries where such initiatives have been discussed or adopted, of which 11 are EU Member States: Austria, Belgium, Denmark, Finland, France, Germany, Italy, Luxembourg, the Netherlands, Sweden and the United Kingdom. The remaining two are Norway and Switzerland, where mandatory due diligence laws would be likely to affect many EU-based companies.[118] Recent trends have witnessed a growing support for mandatory human rights due diligence regulation from certain large multinational corporations.[119]

In parallel, calls for mandatory due diligence legislation at the EU level have started to emerge,[120] including from certain major multinational corporations.[121] In March 2019, the Responsible Business Conduct Working Group ("RBC Group") of the European Parliament presented its *Shadow EU Action Plan* on the implementation of the UNGPs, calling, amongst other things, for the adoption of mandatory due diligence for EU businesses and business operating within the EU.[122] On 3 October 2019, over 80 NGOs and trade unions published a call on the European Commission "for effective EU legislation that establishes a mandatory human rights and environmental due diligence framework for business, companies and financial institutions operating, or offering products or service, within the EU."[123] In November 2019, the European Network of National Human Rights Institutions (ENNHRI)[124] issued a statement to the new European

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[114] Finnwatch,"Finnish Government commits to HRDD legislation', *European Coalition for Corporate Justice*, 3 June 2019, available at: http://corporatejustice.org/news/15476-finnish-government-commits-to-hrdd-legislation.
[115] Open letter to the Italian institutions on the issue of Business and Human Rights, available at: https://www.business-humanrights.org/sites/default/files/Open_letter_B%26HR_English.pdf
[116] Business and Human Rights Resource Centre ("BHRRC"), "German Development Ministry drafts law on mandatory human rights due diligence for German companies", available at: https://www.business-humanrights.org/en/german-development-ministry-drafts-law-on-mandatory-human-rights-due-diligence-for-german-companies. It is noted that the German Federal Government recently issued a statement stressing that the document merely constitutes "internal considerations" within the German Federal Ministry for Industrial Cooperation and Development ("BMZ"), https://www.bundestag.de/presse/hib/670510-670510.
[117] BHRRC, "Mandatory Due Diligence", available at: https://www.business-humanrights.org/en/mandatory-due-diligence.
[118] The 11 EU Member States listed are Austria, Belgium, Denmark, Finland, France, Germany, Italy, Luxembourg, the Netherlands, Sweden and the United Kingdom. The two remaining listed countries are Norway and Switzerland. BHRRC "National movements for mandatory human rights due diligence in European countries", 22 May 2019, available at: https://www.business-humanrights.org/en/national-movements-for-mandatory-human-rights-due-diligence-in-european-countries.
[119] For example, this is the case with the Finnish campaign calling for mandatory human rights legislation in Finland, Finnwatch above n 114, and the Swiss legislative counter-proposal which has received business support, Maude Bonvin, "Entreprises mises devant leurs responsabilités", *Agefi*, 15 June 2018, available at: https://www.gemonline.ch/uploads/_Files/documents_publics/Revue_de_presse/2018/2018.06.15_Agefi_Entreprises%20mises%20devant%20leurs%20responsabilites.pdf.
[120] See below the Section III Regulatory Review on EU-level standard and developments.
[121] Fern, "Chocolate companies and MEPs call for EU Due Diligence Regulation", 10 April 2019, available at: https://www.fern.org/news-resources/chocolate-companies-and-meps-call-for-eu-due-diligence-regulation-954/.
[122] Responsible Business Conduct Working Group, Shadow EU Action Plan on the Implementation of the UN Guiding Principles on Business and Human Rights within the EU, March 2019, available at: https://responsiblebusinessconduct.eu/wp/wp-content/uploads/2019/03/SHADOW-EU-Action-Plan-on-Business-and-Human-Rights.pdf at 6.
[123] European Coalition for Corporate Justice ("ECCJ"), "Civil Society Calls for Human Rights and Environmental Due Diligence Legislation", 3 October 2019, available at: http://corporatejustice.org/news/16785-civil-society-calls-for-human-rights-and-environmental-due-diligence-legislation.
[124] The European Network of National Human Rights Institutions (ENNHRI) is a network which brings together 45 National Human Rights Institutions across wider Europe.

Commission which recommends[125] the development adoption of an EU-level Action Plan on Business and Human rights which should include measures on a "European Human Rights Due Diligence legislation".[126] The ENNHRI notes:[127]

> [T]o enhance legal certainty for both rights holders and businesses and to ensure a level playing field within the EU, the Action Plan should aim at avoiding the creation of an eclectic system of human rights due diligence norms that differ from member state to member state and should instead assess options for an EU-level regulation in this area.

Simultaneously, in the US, the Business Roundtable during August 2019 released a new statement signed by 181 CEOs on the Purpose of a Corporation, which marks a paradigm shift from shareholders to stakeholders focus. The statement affirms a fundamental commitment to the benefit of all stakeholders, including customers, employees, suppliers, communities, as well as shareholders.[128] Meanwhile, in France the so-called "Loi PACTE" of 2019 introduces a requirement for the corporate purpose to be managed "taking into consideration the social and environmental stakes linked to its activity".[129] The December 2019 Communication on the European Green Deal highlights that sustainability should be "further embedded into the corporate governance framework, as many companies still focus too much on short-term financial performance compared to their long-term development and sustainability aspects".[130]

In this context of a growing trend in the direction of mandatory due diligence laws, this study has generated extraordinary interest. We were approached by numerous stakeholders asking to be surveyed or interviewed, and a total of 631 stakeholders responded to the surveys. The level of interest was evident not merely from the high numbers, but also substantively from our discussions, interviews and informational calls and meetings with stakeholders. From the outset, all stakeholders impressed upon us the importance of this study and of possible EU-level regulation on mandatory due diligence.

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[125] ENNHRI, "Recommendations of the new EU Commission: developing and adopting an EU-level Action plan on Business and Human Rights", November 2019, available at: http://ennhri.org/wp-content/uploads/2019/11/ENNHRI-BHR-Statement_EU-Commision.pdf

[126] Ibid at 4.

[127] Ibid.

[128] US Business Roundtable, "Statement on the Purpose of a Corporation", August 2019, available at: https://opportunity.businessroundtable.org/wp-content/uploads/2019/08/Business-Roundtable-Statement-on-the-Purpose-of-a-Corporation-with-Signatures.pdf.

[129] LOI n° 2019-486 du 22 mai 2019 relative à la croissance et la transformation des entreprises, available at: https://www.legifrance.gouv.fr/eli/loi/2019/5/22/2019-486/jo/texte.

[130] Communication from the Commission to the European Parliament, the European Council, the Council, the European Economic and Social Committee and the Committee of the Regions, "The European Green Deal", COM(2019) 640 final, 11 December 2019, at p.17.

Table A: Regulatory options developed in this study

Regulatory Option	Description
Option 1: No policy change (baseline scenario)	No changes in regulation at EU level for companies on undertaking due diligence through the supply or value chain. Expectation that possible legal developments at Member States' level will continue.
Option 2: New voluntary guidelines / guidance	New voluntary guidelines at EU level for companies on undertaking due diligence through the supply or value chain. Voluntary guidelines are not usually legally enforceable, but may influence the standard expected of companies.
Option 3: New regulation requiring due diligence reporting	New regulation at EU level requiring companies to report on the steps they have taken to identify, address, prevent and mitigate any adverse human rights and environmental impacts in their own operations or of third-party business relationships (including the supply or value chain). This may differ from the EU non-financial reporting directive with regard to level of detail and transparency required, and an express focus on risks to people and the planet rather than materiality to shareholders.
Option 4: New regulation requiring mandatory due diligence as a legal duty of care	A new mandatory due diligence requirement at EU level would require companies to carry out due diligence to identify, prevent, mitigate and account for actual or potential human rights and environmental impacts in its own operations and supply or value chain, as a legal duty or standard of care.
Sub-option 4.1: New regulation applying to a narrow category of business (limited by sector)	The above new mandatory due diligence regulation (Option 4), which would only apply to certain sectors.
Sub-option 4.2: New regulation applying horizontally across sectors:	The above new mandatory due diligence regulation (Option 4) which would apply across all sectors.
Sub-option 4.2(a): applying only to a defined set of large companies	The above new mandatory due diligence regulation (Option 4) which would only apply to larger companies.
Sub-option 4.2(b): applying to all business, including SMEs	The above new mandatory due diligence regulation (Option 4) which would apply to all companies, including SMEs.
Sub-option 4.2 (c): general duty applying to all business plus specific additional obligations only applying to large companies	The above new mandatory due diligence regulation (Option 4) consisting of a general duty applying to all business, including SMEs, plus additional obligations only applying to large companies, *for example* additional obligations for large companies relating to the Paris Agreement on Climate Change.
Sub-option 4.3: Sub-options 4.1 and 4.2 accompanied by a statutory oversight and / or enforcement mechanism:	The above new mandatory due diligence regulation (Option 4) accompanied by an oversight and/or enforcement mechanism.
Sub-option 4.3(a): mechanisms for judicial or non-judicial remedies	The above new mandatory due diligence regulation (Option 4) accompanied by mechanisms for judicial and non-judicial remedies
Sub-option 4.3(b): state-based oversight body and sanction for non-compliance	The above new mandatory due diligence regulation (Option 4) accompanied by a State-based oversight body and sanctions for non-compliance.

II. MARKET PRACTICES

1. Introduction

This section examines current market practices for due diligence through the supply chain. It sets out some of the findings of our surveys and interviews within the discussion. Where relevant, it also sets out the relevant findings of a literature review and legal research, including guidance, civil society reports, academic literature, mainstream media, statutes, draft legal proposals and case law. It also contains ten short case studies that highlight interesting examples of some due diligence-related company practices that are discussed in publicly available materials.

The findings in this section should be read in conjunction with the discussion of the existing laws and standards in the Regulatory Review, as well as the regulatory options developed in the Problem Analysis and Regulatory Options.

Please note that the **graphic representations of the survey findings** are set out below in the **PART II Survey Results Statistics**, and key statistical findings are analysed in the Assessment of Options section.

2. Methodology

For the Market Practices section, we undertook two separate surveys, one for companies (hereafter often referred to as **"business" respondents**), and one for all other stakeholders (hereafter referred to as **"general" respondents**), including business associations and industry organisations, civil society, worker representations or trade unions, legal practitioners and government bodies.

The business survey asked specific questions about current due diligence practices, including the costs and benefits of these activities as well as perceived impacts of possible regulatory options on individual companies. Both surveys asked respondents for their views on the existing regulatory framework, and about the likely impacts of the relevant regulatory options.[131] In accordance with the EU Better Regulation framework, sustainability impacts were categorised as social, environmental and human rights impacts.

The surveys were disseminated widely amongst stakeholders across the European Union and worldwide during late March 2019.[132] The original survey deadline was 26 April 2019, which was extended, at the request of stakeholders due to the high level of interest in the study, to 7 May 2019.

We received a total of 631 survey responses, divided between 334 responses to our business survey (with a 28% completion rate)[133], and 297 responses to our general stakeholders' survey (with a 48% completion rate).

In addition to the surveys, we undertook 35 interviews with business and other stakeholders. Of these, 10 interviews were with companies and 25 interviews with other stakeholders, including 7 business-facing organisations, 12 civil society organisations or NGOs, 1 trade union association, 2 government officials, 1 academic, 1 OECD National Contact Point and 1 international organisation. Interviewees are operational across the

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[131] This study did not aim to ascertain whether companies or respondents are advocating for any measure above another. Instead, respondents from a wide range of business and other stakeholders were asked detailed questions about the perceived impacts based on their detailed experience with due diligence.
[132] The survey was disseminated widely across the contacts of study partners, and relevant contacts reported of further distribution amongst their own networks.
[133] Completion rate refers to the number of respondents who completed the entire survey.

EU and the world, and primarily based in Belgium, Finland, France, Germany, the Netherlands, Norway, Spain, Switzerland, Poland, the UK and the US.

Interviews took place between late March and early May 2019. Interviews were anonymous, but where interviewees are named below, they provided permission for these quotes to be attributed to them. In addition to these interviews, we also undertook 15 informational calls or meetings with further stakeholders and experts, including business-facing advisors, business membership organisations, civil society and legal practitioners. The information received during informational calls or meetings informed our findings and, where relevant, anonymous quotes are included. For ease of reference, both interviewees and those stakeholders with whom we undertook informational calls or meetings will be described herein as "interviewees".

In addition, this section analyses current market practices with reference to ten case studies, based on publicly available information. Case studies were selected based on informative examples of how companies are currently undertaking due diligence, how these practices have developed, and some of the challenges which companies face.

This research was supplemented by desktop and legal research, including relevant guidance, civil society reports, academic literature, mainstream media, statutes, draft legal proposals and case law.

3. General survey data

3.1 Business survey respondents

Business respondents were spread relatively even across sectors,[134] with the top six most represented sectors being manufacturing (20.66%), automotive (12.28%), IT and technology (10.48%), financial services (9.88%) consumer goods (9.58%), and agriculture and agribusiness (8.68%).[135] Business respondents represented enterprises of all sizes. Of those business respondents which operate in agriculture or agribusiness, 38.1% operate in coffee, 38.1% in cocoa and 9.52% in tea. Over half (52.38%) selected other agricultural subsectors, the most predominant of which included oilseed, grain, tobacco, cotton, wheat, fruit, vegetable seeds, sugar and equipment for agriculture.

The majority (65.90%) of respondents are large multinational companies with 1000 or more employees, but SMEs were also represented: 9.58% respondents have 50 to 249 employees, and 7.66% have 0 to 9 employees. Following this, 7.28% of respondents have 500 to 1000 employees, 6.51% have 250 to 500 employees, and 3.07% have 10 to 49 employees. Business respondents estimated that they had, in total, over 3 million[136] first tier suppliers, and over 1 billion suppliers in the upstream supply chain.[137]

For simplicity, SMEs for the purpose of this study will be defined with reference to the number of employees specified by survey respondents, in accordance with the following thresholds contained in the EU definition of SMEs in EU recommendation 2003/261:[138]

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[134] These sector categories were agreed in terms of the inception report as part of the business and general survey questionnaires.
[135] Of those business survey respondents who selected agriculture and agribusiness, 36.36% operate in coffee and 36.36% operate in cocoa, with 9.09% operating in tea, and the remaining 54.55% operating in other areas of agriculture.
[136] Total estimated number of all respondents' first tier suppliers: 3,293,716.
[137] Total estimated number of suppliers in all respondents' entire upstream supply chains: 1,059,375,426. Total estimated number of business enterprises in all respondents' entire value chain (including upstream and downstream) : 1,066,565,386.
[138] EU Commission Recommendation of 6 May 2003 concerning the definition of micro, small and medium-sized enterprises (Text with EEA relevance) (notified under document number C(2003) 1422), available at: https://eur-lex.europa.eu/eli/reco/2003/361/oj. It is noted that our references to SMEs in this section relates to employee numbers rather than turnover, and that the accuracy of the information regarding number of employees provided by the individual survey respondents was not verified.

Micro: 10 or less employees
Small: 50 or less employees
Medium-sized: 250 or less employees

Where relevant below, and particularly relating to current due diligence practices and views on regulatory options, business survey responses are presented with reference to the company size by number of employees. It should be noted that the samples of micro, small and medium company respondents are significantly smaller than those of respondents with 1000+ employees. Where breakdowns by company size are not provided, it should be assumed that these findings either follow the general overall trends, that breakdowns by company size are not significantly revealing or relevant, or that sample sizes are too small. Analysis by company size are discussed in further detail in the Assessment of Options section.

Business respondents operate across the EU and the world, with 2.86% of business respondents indicating that they only operate outside of the EU, and 15.32% of respondents indicating that they only operate within the EU.[139] Business respondents operate in all Member States, insofar as each Member State was selected by at least 40 business respondents.

The primary base or headquarters of business respondents were spread across EU Member states, with the majority being based in Germany (39.09%), followed by France (10.75%), Sweden (8.79%), the Netherlands (6.51%), the UK (5.54%),[140] Spain (4.56%), Finland (4.23%) and Italy (4.23%). Of business respondents, 13.36% are primarily based outside of the EU, of which most are in Switzerland, followed by the USA, and thereafter Japan and Australia. No business respondents selected Bulgaria, Cyprus, Hungary or Romania as their primary base.

The majority of business respondents were from the corporate social responsibility (29.24%) or sustainability (22.22%) functions within their companies, followed by legal (9.36%) and procurement or supply chains (8.19%). 7.02% were Directors. Within micro survey respondents with 9 or less employees, 50% of respondents were CEOs.

Business respondents with 1000 employees or more were predominantly multinational: of the 38 respondents 1000+ employee respondents which indicated that they operate only within the EU, only three operate exclusively in one member country (i.e. are very large national companies rather than a multinational). Only 2.86% of 1000+ employee respondents indicated that they only operate outside of the EU, and of these all are multinational, with many operating in large or multiple regions which are different from where they are headquartered. For the purposes of the analysis in this section, we accordingly refer to large or 1000+ employee companies as multinationals, particularly where the publicly expressed views of multinationals are under consideration.

3.2 General survey respondents

About half (50.17%) of general respondents were from civil society, followed by industry organisations (21.89%). Other groups were significantly smaller: public authorities or government departments were 5.39%, legal practice corporate advisors were 4.38%, trade unions or worker representation were 4.38%, and legal practice claimant advisers were 4.04%.Three respondents were from OECD National Contact Points, two from national human rights institutions, one from a labour inspectorate, and one from an environmental inspectorate.

[139] Of micro respondents with 9 or less employees, 47.06% indicated that they only operate within the EU.
[140] In light of uncertainty around the UK's leave from the European Union, the UK was listed in the survey as both a Member State, in square brackets, and in the question about operating outside of the EU.

The views of the top two most represented general stakeholder groups, namely civil society and industry organisation respondents, were often quite contrasting. For key questions below, the views of these two stakeholder groups are presented by stakeholder group, in addition to the general stakeholders' views.

Insofar as industry organisations represent significant numbers of business members of all sectors, sizes and operating contexts, and were the second largest stakeholder group amongst general stakeholder respondents, their views are discussed in this survey as representative of a broad base of business. Indeed, although the survey was anonymous, industry organisations frequently identified themselves in their responses (many of which were detailed and considered). From this identification it is evident that industry organisations represented a comprehensive and persuasive range of business views. For example, one industry organisation respondent alone represents 8000 companies with €7.6 trillion market capital, and another has over 16 000 member companies.

The views of industry organisations are in key places compared and contrasted with the views of civil society stakeholders. Moreover, in some instances the views of business respondents, particularly multinational companies, are notably different from those of industry organisations. Where this is the case for key questions, these contrasting views will be highlighted.

The most (39.70%) general stakeholders indicated that their work is not sector-specific or spans across sectors. Of those who do work on specific sectors, the most (35.21%) work in agriculture and agribusiness. Of these, over two thirds (67.47%) work in cocoa, 33.73% in coffee, and 30.12% in tea. After agriculture, the most selected sectors by general respondents were mining and quarrying (22.85%), consumer goods (22.10%), manufacturing (19.10%) and financial services (14.61%). General survey responses cover all of the sectors in their work: all of the sectors on our list were selected by at least five respondents.

Half of civil society respondents indicated that their work focuses on agriculture and agribusiness (50.74), followed by over a third which indicated that their work is not sector-specific or cuts across sectors (36.76%). Just under a third (30.15%) of civil society respondents work in the area of mining and quarrying, and just under a quarter in consumer goods (23.53%). Of those working in agriculture, 65.08% work in cocoa, 36.51% in coffee and 30.16% in tea. Almost two thirds (65.08%) also work in other agricultural subsectors, the most prominent of which were palm oil, beef, soy, sugar, rubber, banana, cotton, and timber.

Just over a third (35.71%) of respondents from industry organisations indicated that their work is not sector-specific or cuts across sectors, followed by manufacturing (32.14%), consumer goods (19.4%) and agriculture and agribusiness (16.07%). Of those who selected agriculture, four respondents work in cocoa, one in tea and one in coffee. One works in palm oil and soy.

General stakeholders work with companies that are primarily based in all EU Member States: all of the Member States were selected by at least 17 respondents. The most frequently selected Member State in terms of company headquarters was Germany (40.24%) followed by the UK (36.65%), the Netherlands (29.08%), France (26.69%) and Belgium (23.11%). 31.47% of general respondents indicated that they work globally, or with companies primarily based outside of the EU, particularly Switzerland and the US. Other countries which were mentioned as being the primary base of companies which general stakeholders work with include (alphabetically) Argentina, Australia, Bangladesh, Brazil, Cambodia, Cameroon, Canada, China, Colombia, Côte d'Ivoire, DRC, Guatemala, Guyana, India, Indonesia, Japan, Kenya, South Korea, Lebanon, Liberia, Malawi, Malaysia, Nicaragua, New Zealand, Nigeria, Norway, Paraguay, Peru, Singapore, South Africa, Sri Lanka, and Suriname.

Similarly, general stakeholders' work cover countries which operate across EU Member States and the world: all EU Member States were selected by at least 37 general respondents. The top most selected EU Member States by general stakeholders with respect to where the companies covered in their work are operating were Germany (42.32%), the UK (38.17%), the Netherlands (36.51%), France (33.61%) and Italy (29.46%).

The vast majority of general stakeholders also indicated that companies relevant to their work operate outside of the EU. Of these, 70.54% work on companies that operate in Asia (excluding India and China), 62.05% in Latin America (including Mexico), 57.14% in China, 56.7% in Sub-Saharan Africa, 54.02% in India, and 47.77% in the US and Canada. Only 16.96% of respondents indicated that companies relevant to their work operate mainly within the EU.

General respondents' work covers companies of all sizes, with the majority (56.50%) indicating that their work relates to large companies with 1000 or more employees.

4. Current due diligence practices

In accordance with the TOR, our discussion of current business practices for due diligence will take place within the framework of the four components of due diligence as set out in the UNGPs,[141] namely:

1. Identifying and assessing actual or potential adverse impacts
2. Taking integrated action to address these impacts
3. Tracking the effectiveness of those actions taken, and
4. Communicating how impacts are addressed.

The findings of the empirical evidence and analysis will be supplemented, where relevant, by ten case studies which demonstrate real-life examples of certain practices.

4.1 Overview of current practices

Survey respondents were asked questions about whether companies are currently undertaking due diligence for human rights and environmental impacts, and if so how they are doing this within their own operations and supply chains. Moreover, survey respondents were asked what language is used for these processes, and whether due diligence covers climate change and wider social issues.

Of business respondents, 37.14% are undertaking due diligence which takes into account all human rights and environmental impacts (but as noted below, only about 16% cover the entire value chain). This is closely followed by 33.71% which currently undertake due diligence only in certain areas (for example health and safety, labour, non-discrimination and equality, environmental, land rights and indigenous communities).

Only 7.43% indicated that they are currently undertaking environmental or climate change due diligence which does not extend to other human rights. The same number, 7.43% of respondents, indicated that they do not and have not undertaken any form of due diligence for any human rights or environmental impacts.

[141] UNGP 17.

These trends are similarly reflected in respondents companies with over 1000 employees, 42.98% of which conducts "[h]uman rights due diligence which takes into account all human rights (including environment)", and 38.84% undertake this due diligence only in certain areas. Within these large companies, only 4.96% indicated that they undertake environmental or climate change due diligence which does not extend to other human rights. Within large companies, only 2.48% do not currently undertake any form of due diligence.

Although the samples are smaller, survey results suggest that current due diligence practices within SMEs are slightly less established. Of micro respondents with 9 or less employees, 60% indicated that they did not know whether their company undertakes due diligence, which is notable insofar as 50% of this size group indicated that they are CEOs. Moreover, 20% indicated that their company does not or has not undertaken any form of due diligence for human rights or environmental impacts. Of medium-sized respondents with 50 to 249 employees, 33.33% undertake "human rights due diligence which takes into account all human rights (including environment)", and 27.78% undertake such due diligence only in certain areas. 16.67% undertake environmental or climate change due diligence which does not extend to other human rights, and 16.67% indicated that their company does not currently undertake due diligence for these impacts.

It should be noted that these are respondents' self-reported perceptions on their companies' due diligence practices. These should be considered within the broader background of the general stakeholders' responses discussed below, as well as external reports regarding corporate due diligence practices, which generally show lower figures of implementation in relation to existing corporate implementation of due diligence. A growing body of evidence exists about the current due diligence practices of companies for their human rights and environmental impacts, which is discussed in further detail in the Problem Analysis and Regulatory Options section.

For example, a 2016 study carried out by BIICL and the law firm Norton Rose Fulbright revealed that the majority of companies are failing to undertake human rights due diligence, with over half of surveyed companies[142] having never had a dedicated human rights due diligence process in place. The report highlighted that, as a result, companies are failing to identify potential or actual adverse human rights impacts in their activities and throughout their value and supply chains.[143] It showed that those companies which undertake non-specific due diligence (not expressed in human rights terms) in accordance with existing regulated areas such as health and safety and labour laws were failing to identify and address other risks outside of these areas.

Similarly, in 2018, the Corporate Human Rights Benchmark assessed 101 of the largest publicly traded companies in the world across three industries (agricultural products, apparel and extractives).[144] The findings of the assessment depict a "deeply concerning" picture, with the majority of companies scoring poorly on the Benchmark,[145] and 40% of companies scoring no points at all across the human rights due diligence section of the assessment.[146]

[142] The study surveyed 152 major companies working across various sectors.
[143] The BIICL study was published as Robert McCorquodale, Lise Smit, Stuart Neely and Robin Brooks, "Human Rights Due Diligence in Law and Practice: Good Practices and Challenges of Business Enterprises" (2017) 2 *Business and Human Rights Journal* 195–224.
[144] The Corporate Human Rights Benchmark ("CHRB") is a collaboration led by investors and civil society organisations dedicated to creating the first open and public benchmark of corporate human rights performance, available at: www.corporatebenchmark.org.
[145] CHRB, "2018 Key Finding - Apparel, Agricultural Products and Extractive Companies", 2018, available at: https://www.corporatebenchmark.org/sites/default/files/documents/CHRBKeyFindings2018.pdf at 5.
[146] Ibid at 13.

As this study was being finalised, the findings of the 2019 CHRB assessment were published, which show similar results. They indicate that "human rights due diligence is a key weakness for most companies",[147] with companies scoring on average 21% (3.2 out of 15) under the human rights due diligence assessment area, and nearly half (49%) of the companies assessed (which were doubled in 2019) scoring zero against every human rights due diligence indicator.[148] It is noted that the CHRB relies on public reports to allocate these scores, which again highlights the concern raised by stakeholders that there are discrepancies between companies' public reports and what they are doing in reality.

In a similar vein, a recently published report focusing on Irish companies's engagement with business and human rights revealed a weak performance of Irish companies across the board, and identified a particular weakness in the area of embedding respect for human rights and human rights due diligence, with companies scoring an average of just 2% on human rights due diligence.[149]

One interviewee in an organisation which works with companies on their due diligence practices, particularly in their supply chains, described the current situation as follows:

> It feels like we are essentially offshoring exploitation…European countries have essentially outsourced that, relocated factories to countries where the cost of production is very low and where governance [is actually] problematic, and recreated that industry.
>
> They're sourcing from places where they know these conditions would be prohibited at home. No payment that meets minimum wage or very, very long working hours, and working in structurally unsound factories or whatever it might be. The unfair labour practices continue. They're just going on in places where local governments are unable or unwilling to import domestic or international labour rights legislation.

4.2 Scope of due diligence

Whether due diligence practices currently include environmental and climate change due diligence?

As will be seen below, the vast majority of business stakeholders expressly include environmental impacts in their due diligence, and many others view environmental impacts as implied as included.[150]

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[147] CHRB, "2019 Key Findings - Across sectors: Agricultural Products, Apparel, Extractives & ICT Manufacturing, available at: https://www.corporatebenchmark.org/sites/default/files/2019-11/CHRB2019KeyFindingsReport.pdf, at 8.
[148] Ibid at 8.
[149] B. Finlay Hogan, M.L. Rhodes, S.P. Murphy, and M. Lawlor, "Irish Business & Human Rights: Benchmarking compliance with the UN Guiding Principles", Centre for Social Innovation, Trinity Business School, 8 November 2019, available at: https://www.tcd.ie/business/assets/pdf/CSI-BHR-Report-1.pdf
[150] It is noted that both the BIICL study above n 143 and the CHRB report ibid focused on human rights due diligence which covers all human rights, whereas the survey for this study included other categories of due diligence such as those relating to other areas only, and exclusive environmental due diligence. In a later part of the survey, discussed below, survey respondents were asked about their preferences for different regulatory options. This included a question about "issue-specific" regulation which covers only one specific human rights or environmental issue. Although this question was not specifically about the inclusion of environmental impacts in current due diligence practices, some comments from business survey respondents were relevant. For example:
- "There could be merit in considering all human rights in one harmonised way rather than one human right at a time. Including all environmental impacts in the same may prove to be too challenging and needs to be considered whether they go naturally hand in hand or whether it becomes very difficult to implement. The process of due diligence is similar for both."
- "The UNGP lay the foundation and are clear in acting upon all recognised human rights. At the same time, the concept of including (all) environmental impacts, is not elaborated yet. As long as human rights are also to be seen with environmental impacts, these are covered. However, on environmental impacts in general, lots of literature, advice and regulation exists. To put everything in one concept does not help to clarify things, but in my view, distracts from the main issues. Therefore I would recommend at the moment to view the issues in a holistic way, without blurring (established) concepts. Also, you may consider that different people/ departments are in general responsible for environmental issues and human rights due

Given the mandate of this study, survey respondents were also asked specific questions regarding due diligence for climate change impacts. Although survey respondents indicated that the term "climate change due diligence" is currently rarely used as a self-standing form of due diligence (see below), business respondents indicated that environmental impacts including aspects of climate change, air pollution and greenhouse gas emissions are viewed by business survey respondents as included, either expressly or implied, within existing due diligence processes.

When asked which aspects are currently expressly included in their due diligence, or "implied as included (though not expressly mentioned)", business respondents indicated that environment is expressly included (85.84%) or implied as included (14.16%). Air pollution and greenhouse gas emissions are expressly included (77.88%) or implied as included (22.12%), and climate change is expressly included (60.20%) or implied as included (39.80%). Biodiversity is expressly included by 44.83% or implied as included by 55.17%.

These trends were even more pronounced within large companies with over 1000 employees: The top issues selected as "expressly included" within their due diligence processes were labour rights (selected by 90 respondents out of the 100 which responded to the question), non-discrimination and equality (85 respondents), health and safety (83 respondents), environment (75 respondents), air pollution / greenhouse gas emissions (65 respondents) and climate change (49 respondents). Top issues selected as "implied as included (though not expressly included)" were land rights (40 respondents), indigenous communities (37 respondents), biodiversity (35 respondents), profit-shifting to low tax jurisdictions (33 respondents), climate change (28 respondents) and income inequality (28 respondents).

It is interesting to note that a relatively large proportion of large (1000+ employees) business respondents view climate change and air pollution / greenhouse gas emissions as expressly included in their due diligence processes, and just under a third view climate change as implied as included.

An international and comparative environmental law expert, Ivano Alogna, who specializes in the legal models used for environmental regulation, explained in an informational call that there is currently a "bricolage" of legal instruments aimed at the protection of the environment:

> It is a history made of principles influencing legal instruments, soft law hardening such as from voluntary CSR to hard law obligations, and an enormous amount of legal tools for the protection of the environment...Yet, I believe that currently, the first and only example of legislation which requires companies to exercise a 'duty of vigilance of parent and outsourcing companies' for environmental harm is the French [Duty of Vigilance] Law. Other environmental laws or standards are either soft law instruments, or they apply legal duties to States...The French law is the first legislative model worldwide that places the burden of responsibility of prevention on the multinational company, which incurs its civil liability for its activities and environmental externalities...Considering the recognized importance of a legally binding instrument to regulate the activity of transnational corporations, stressed in particular by the efforts made by the UNHRC in this direction, this new legal model may offer a solid foundation to draft a European instrument of this kind.

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diligence. Collaboration is needed and needs to be improved, yet realistically this will take some time. Human rights due diligence, though the UNGP in its 8th year, are still a "new" concept for most businesses, and other stakeholders alike."

Interviewees also suggested that insofar as climate change impacts have impacts on people (also in the long run), they are already viewed within scope of human rights due diligence as it originated from the UNGPs. An interviewee from an international civil society organisation indicated:

> We have only really just begun to look at the relevance of due diligence for tackling climate change. And it has been and it will always be in relation to the human rights impacts of climate change and the contribution of companies, most probably fossil fuel companies, to those human rights impacts as a consequence of their failure to reduce their greenhouse emissions, to reduce their reliance on fossil fuels, to shift to clean energy etcetera…

The interviewee continued to highlight that insofar as the focus is on what the company can do to address its impacts, due diligence responsibilities extend to climate change impacts:

> What I would say for sure is that the extent to which you can link a company's failure to do what is within its remit to do, to tackle climate change, and that leads to a negative impact on human rights, we would consider that to be within the remit of their due diligence responsibilities.

Another interviewee from an international civil society organisation also highlighted that the UNGPs concept of due diligence is a methodology by which a company should identify, assess and address its impacts on people. This same methodology may potentially be used to address questions about environmental harms, including climate change:

> I think we have to distinguish between due diligence as an instrument, and then what kind of risks the instrument has to identify. And so what kind of process, and whether the process would actually change as part of what kind of risks are we looking at. [T]he particular part of human rights due diligence is, for instance, the specific role of the rights-holder, so communities and the part of the instrument that uses consultations and engagement with the stakeholders to identify but also mitigate risks…
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> But due diligence as such, the idea of having due diligence embedded in management structures, having a process in place to identify specific risks, in this case the human rights, the basic methodology is the same. But the UNGPs provide a framework for particular human rights risks where you have people, communities, stakeholders as part of the methodology.

An interviewee from another civil society organisation, which is currently campaigning for mandatory due diligence in an EU Member State, stated:

> I would actually challenge the view that an environmental impact does not have a human rights impact. I think it pretty much always does. Even if it's not an immediate impact. Even if it's not: 'There was pollution and I cannot farm on my land anymore'. At perhaps a couple of steps removed, there is always an impact. And obviously in climate change there is an impact on everyone, arguably.

The interviewee highlighted that many of the groups which are working on environmental issues are in fact focused on the environmental impacts on people:

> There is whole group of people working on deforestation, but the primary reason that they are interested in that is because of the impacts it has on people that rely on forestry for their livelihoods. So again you can make the connection to human rights and that's what we would do.

The idea that companies have responsibilities for their climate change impacts are not new. For example, in 2018 the UN Climate Change Secretariat has proposed a fashion industry charter for climate action,[151] which was supported by Stella McCartney, who stated: "What is essential is for the big players in the industry to come along with me, because that changes the price point."[152] Similarly, although the Paris Agreement applies to States, it contains a workstream regarding how business and states can work together.[153]

However, until recently, it has not been clear how an individual company's due diligence should include its impacts on climate change. It was seen to be difficult to ascribe proportional responsibility to one company for something that has global contributors.

For example, an interviewee who is a legal expert on the development of the Swiss Responsible Business Initiative proposal for mandatory due diligence legislation was of the opinion that climate change litigation would most probably not be included within scope of that law, "due to the very unclear scope of what climate change can be". They indicated that the Swiss legal proposal would be "more focused on civil damages and civil remedies that we already know."

Another interviewee added that legal duties for due diligence regarding the environment can be "quite different to what we are talking about here, because it's very vague in terms of how you would actually assess as whether you had fulfilled that duty or not and how you would be held to account for not doing so." They added:

> With climate, a lot of the efforts have gone into things like reducing resource use and reducing carbon emissions. But people think that that has only taken them so far, and now they are looking at things like the climate litigation. The question for them is how to you deal business activities that are fundamentally not sustainable, the oil industry for instance.

Perhaps for these reasons, due diligence practices for human rights and climate change respectively have to a certain extent developed in "silos" within companies. An interviewee from a multinational food and drink company indicated about their company's due diligence work, which they call "human rights due diligence":

> In terms of scope of the substance, the issues, we are really focused on human rights, on the Universal Declaration of Human Rights and the relevant Conventions. So I would say that while we have been able to look at impact of environmental issues on people, we have not carried out per se like a climate change due diligence process, I would say, at least not as part of the human rights due diligence programme. Now, of course, you know, we have people working in operations, that actually look after climate change in particular…Really trying to understand better [the] Scope 1, 2, 3 emissions, and we are engaging with suppliers. But this is quite separate from our human rights due diligence programme.

One interviewee from a multinational garment company indicated, with respect to the company's environmental and human rights due diligence teams:

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[151] UN Climate Change, "Fashion Industry, UN Pursue Climate Action for Sustainable Development:, 22 January 2018, available at: https://unfccc.int/news/fashion-industry-un-pursue-climate-action-for-sustainable-development.

[152] Jess Cartner-Morley, "Stella McCartney to launch UN charter for sustainable fashion", *The Guardian*, 29 November 2018, available at: https://www.theguardian.com/fashion/2018/nov/29/stella-mccartney-to-launch-un-charter-sustainable-fashion.

[153] Samantha Harris, "Ambitious Climate Action Before 2020, Business Should Focus on 'Workstream 2'", *BSR*, 5 June 2015, available at: https://www.bsr.org/en/our-insights/blog-view/for-ambitious-climate-action-before-2020-business-should-focus-on-workstrea.

> We are from the same area, same department [sustainability], we do have similar processes. We started together, we have developed internal tools. These tools are shared in the environmental and social or human rights teams, and also used by our commercial colleagues, the ones that buy the garments. The type and process of due diligence is quite similar. Same scopes, same visibility…
>
> In my company, we are pushing it from the social sustainability department towards the rest of the company and their processes and areas of the company: human resources, logistics, distributions centres, in our stores, etcetera. Because for us, in our sector, it makes sense. We have been building almost two decades of expertise in due diligence in human rights, even from before the Guiding Principles were out. So we have our own processes of due diligence, and our ways of calling it. And what we have been doing since 2011 is making sure that our own processes are aligned with the Guiding Principles, and we have been trying to understand if what we are doing is enough. So with that expertise that we have from the human rights part of the supply chain, the company understood that the mandate to extend the due diligence to the rest of the company should come from our area. So this is what we are doing, and I am the person responsible for doing that.

The interviewee further explained:

> Environmental covers the whole cycle: supply chain and logistics, eco-efficient stores, recycling, second life of the product. They have a circular, and then our paths cross when it comes to supply chain, and there we work together.

An interviewee from a company which has undertaken dedicated due diligence in its supply chain indicated:

> One of the things that we do is a life-cycle assessment on our products. Which means that we look at different tiers of the supply chain and their emissions of greenhouse gases, and different aspects of where the impacts are and where our environmental footprint is the biggest. And that goes all the way from the materials that are used to the actual used phase of the product. And there is also the energy used, repairs that needs to be done, etcetera. In that full life-cycle, we focus mostly on where we can have the most influence. Which is actually in the used phase, so designing products that actually are facilitating repairs. So people don't throw away, but can reuse parts as much as possible.

The interviewee further added:

> There are examples of other manufacturers that do life-cycle analysis but I don't think it is common practice.

As discussed in the Regulatory Review section, very recent developments indicate that the understanding of how precisely climate change impacts can form part of due diligence is evolving rapidly. For example, during the course of the empirical phase of this study, the OECD National Contact Point in the Netherlands for the first time clarified how climate change targets can be understood as being expressly part of a company's due diligence responsibilities.[154] As a result of these developments, there seems to be a growing acknowledgement that climate change impacts are to be viewed within the company's own due diligence responsibilities.

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[154] The Netherlands National Contact Point for the OECD Guidelines for Multinational Enterprises, *Oxfam Novib, Greenpeace Netherlands, BankTrack and Friends of the Earth Netherlands (Milieudefensie) versus ING*, Final Statement, 19 April 2019, available at: https://www.oecdguidelines.nl/documents/publication/2019/04/19/ncp-final-statement-4-ngos-vs-ing. See discussion in Regulatory Review.

These developments are also taking shape within business. At the April 2019 Sustainable Europe 2030 conference, Saori DuBourg of BASF indicated:[155]

> "What I see right now, and this is true for the entire industry, there is a concern that increasing effort from the industry…how can we now go further to really meet the Paris Protocol?"

Other recent developments in this regard include:

- On 17 June 2019, the *Financial Times* published an article on a new metric by Carbon Delta, which analysis how companies are addressing their climate change impacts, including how they are meeting their own targets set in response to the Paris Agreement. The article starts by stating that: "It has been a big week for climate change — and the companies trying to tackle it."[156]

- Also on 17 June 2019, 88 investors worth almost US$10 trillion indicated that they will push for more disclosure on environmental impacts, including climate change, water and deforestations.[157]

- On the following day, 18 June 2019, the EU published its Non-Binding Guidelines on corporate Climate-related information reporting, which indicate that in terms of reporting under the EU non-financial reporting directive, "climate-related information can be considered to fall into the category of environmental matters".[158]

- On 25 June 2019, a report from the UN Special Rapporteur on extreme poverty and human rights reaffirmed the impact of climate change on human rights in no uncertain terms. The report criticises states and other actors for "giving only marginal attention to human rights in the conversation on climate change"[159] for decades, and that "as a full-blown crisis bears down on the world, business as usual is a response that invites disaster".[160] It emphasises the role to be played by companies, alongside other actors, in providing and implementing solutions to climate change, [161] through "a radically more robust, detailed, and coordinated approach".[162]

- A July 2019 report by ClientEarth and Global Witness makes the case for "a generalised due diligence obligation on all EU-based companies providing goods or services in the EU (including financial activities)".[163]

- The Task Force on Climate-Related Financial Disclosures provides companies with recommendations for climate-related financial disclosures. It is a voluntary reporting

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[155] Saori DuBourg, BASF, presentation at *Conference on Sustainable Europe 2030: From Goals to Delivery*, 8 April 2019, Brussels, video available at: https://ec.europa.eu/epsc/events/sustainable-europe-2030_en?pk_source=participants_list&pk_medium=email&pk_campaign=sdg-conf.
[156] Leslie Hook, "World's top 500 companies set to miss Paris climate goals", *Financial Times*, 17 June 2019.
[157] CDP, "Group of 88 investors target over 700 companies for not reporting environmental information", 17 June 2019, available at: https://www.cdp.net/en/articles/media/group-of-88-investors-target-over-700-companies-for-not-reporting-environmental-information.
[158] EU Guidelines on non-financial reporting: Supplement on reporting climate-related information, C/2019/4490 of June 2019.
[159] Report of the Special Rapporteur on extreme poverty and human rights, "Climate change and poverty", A/HRC/41/39 (July 2019), available at: https://documents-dds-ny.un.org/doc/UNDOC/GEN/G19/218/66/PDF/G1921866.pdf?OpenElement at 1.
[160] Ibid at 3.
[161] Ibid.
[162] Ibid at 1.
[163] ClientEarth and Global Witness, "Strengthening Corporate Responsibility: The case for mandatory due diligence in the EU to protect people and the planet", July 2019, available at: https://www.globalwitness.org/en/campaigns/forests/strengthening-corporate-responsibility/ at 14.

initiative aimed at generating information relating to climate impacts that are "consistent, comparable, reliable, clear, and efficient, and provide decision-useful information to lenders, insurers, and investors".[164]

- In September 2019 an investor statement coordinated by UN Principles for Responsible Investment (PRI) called on investee companies to take disclose and implement "quantifiable, time-bound commitments covering the entire supply chain and sourcing geographies" relating to their deforestation impacts in the context of climate change.[165]

- During November 2019, the European Investment Bank has announced that as of the end of 2021 it will no longer finance most fossil fuel projects.[166]

Given the recent nature of these developments, they are likely to not have influenced the findings of our empirical study, which took place during or prior to many of these developments. However, their implications for the evolving understanding of corporate due diligence expectations are discussed in the Regulatory Review section.

Whether due diligence practices currently include due diligence for wider social aspects such as income inequality and profit-shifting to lower tax jurisdictions?

Of business survey respondents, 54.76% indicated that income inequality is expressly included in their due diligence, and 45.24% that it is "implied as included (though not expressly mentioned)". Profit-shifting to lower tax jurisdictions is expressly included in 25.8% of business respondents' due diligence, but in 74.15% it is implied as included.

However, questions as to how to link these wider social impacts with company's own individual impacts and due diligence efforts are still relatively new. An interviewee who works with businesses in the implementation of the UNGPs indicated that:

> The majority of companies that we're dealing with are still struggling with some of the human rights impacts that we would consider very familiar. But the minute you talk about income inequality and inequality more broadly, certainly we see that as going hand in hand with the negative impacts we see as a result of globalization and we see just [a] general trend of how societies are operating and distributing income. And so, issues like living wage are really moving up the agenda quickly. We've done quite a bit of work to emphasize from an SDGs perspective how this is an issue that, if you want to talk about transformation at scale, don't just talk about inventing new social products and services, look at how you can drive a living wage through your entire supply chain. That would be utterly transformational. Nobody is doing that really right now. Which comes back to where I started, about: Are you actually willing to make the decision that this may have some business costs for you in order to really get to better outcomes? So I think the inequality piece is very closely connected, and we're often trying to explain to companies or help them see how addressing negative impacts is just the other side of the coin to what the SDGs are calling for. And of course for many companies the SDGs are a driver at the moment.

An interviewee from an international network of NGOs which promotes corporate accountability with a particular focus on the OECD Guidelines, stated that:

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[164] Task Force of Climate-Related Financial Disclosures, available at: https://www.fsb-tcfd.org/about/.
[165] UN PRI, "Investor statement on deforestation and forest fires in the Amazon" September 2019, available at https://d8g8t13e9vf2o.cloudfront.net/Uploads/g/i/u/investorstatementondeforestationandforestfiresintheamazon_76915.pdf.
[166] "European Investment Bank drops fossil fuel funding", *BBC News*, 14 November 2019, available at: https://www.bbc.co.uk/news/business-50427873.

> Fiscal planning and fair taxes is included in the OECD Guidelines as a Chapter, and there has been an increasing attention to responsible tax practices and fair payment of tax as a corporate accountability issue. Though, interestingly the tax Chapter is explicitly excluded from the due diligence requirements in the OECD Guidelines.

One interviewee working for a multinational company indicated:

> We are not looking at this stage as to whether our tax footprint is related to those topics. If any companies are thinking that way, they are a small minority.

Again, interviewees indicated that whereas wider social impacts are not always expressly included, a due diligence process that focuses on the company's impacts on those affected may well need to focus on wider social impacts. After explaining that the starting point of any mandatory due diligence regulation should be the UNGPs, for clarity, an interviewee from an international food and drinks company explained:

> So this is one thing. Now, having said that, over the years, what we have seen, your due diligence itself, in terms of identifying risks and impacts, even though you actually do focus on, I would say, pure human rights issues, actually remediation activities lead you into territories that go much further than just the human rights framework. I always use the example of child labour, which is a quite specific issue, well-defined by the ILO Conventions, and so forth. But then, when it comes to remediation, if the company actually decides…like in our case if we decide to go into remediation for different reasons, that actually leads us into activities that relate to school building, improving access to education, that actually go, in my view, much further than just the human rights framework, that actually have a direct connection and link with the SDGs and developmental agenda. And I think this is important to recognise that.
>
> But it's more as part of the remediation than as part of the process, I would say. Because if you start too broad with the identification or assessment process, I think you will lose a lot of companies, and also a lot of clarity in terms of what you expect from them.

A few interviewees highlighted that issues such as tax and profit-shifting are usually already highly regulated, including in criminal law. They raised the point that a new regulatory mechanism which provides for a civil remedy or a due diligence defence, should not be used to override and water down existing criminal law provisions. An interview from civil society which is campaigning for a national-level mandatory due diligence law explained:

> Someone said we should be explicit in our materials that it does include tax avoidance, and that it includes anti-corruption measures as well. Again, I would say that it does, because those things have human rights impacts. But I think part of the reason that it has not been in there explicitly up until now is again just to do with the fact that these movements have been separate. It's kind of a siloing issue. There has been a big NGO movement on tax. It's a very complex area. People are only just beginning to conceive of tax evasion as a human rights issue. So whether you would need to be explicit about that or not, you would need to think quite carefully…because if the accountability model is civil liability, then can you use that to hold them to account for non-payment of tax? That's where it becomes tricky.

When asked whether some large issues like tax and income inequality can only be addressed at government or policy level, rather than by individual companies, the interviewee added:

> We need to be slightly careful about that. Some sectors will need to get together and work together where there is an endemic problem, and see where they can work with governments on something that is at a very macro level like tax. There are associations of businesses that are serious about tax, climate, but ultimately that is a policy issue.

It is also noted that the social, environmental and human rights impacts of corporate taxation are complex and contested. A recent study for the European Economic and Social Committee found that:[167]

> There is a wide consensus that part of the corporate tax is passed on to people other than the shareholders. The IMF has noted that 'workers, not shareholders, bear the real incidence of the corporate income tax.' Studies find the tax burden on workers of corporate tax ranges from 30% to 400%. But much public discussion fails to acknowledge the importance of incidence. Neither the European Commission's Communication on the digital tax or the accompanying 161-page impact assessment contain the word 'incidence'.

The study also refers to a study by Fuest et al (2017) which notes that "higher taxes reduce wages most for the low-skilled, for women, and for young workers".[168] These impacts fall outside the scope of this study. However, we note that for these reasons, caution should be taken when considering the extension of due diligence to corporate tax questions.

Case study: BASF and Value-to-Society

BASF is a multinational chemical company headquartered in Germany. The company has developed what it calls the "first monetary assessment of the economic, ecological, and social impacts of its business activities along the value chain".[169] The model, which it calls Value-to-Society, measures in euros the value of BASF's activities along its supply chain.[170]

The model aims at being pragmatic, scalable, transferable and auditable in a way that allows the company to monitor its externalities in a transparent manner.[171] BASF's objective is to allow the public to understand the company's impact from the model's figures.

The scope of the model includes both direct and indirect suppliers, the company's own operations, and customer industries in the downstream value chain.[172] Further, the model classifies impact in different categories, such as profits, taxes, wages, human capital, health and safety, air pollution, greenhouse gases, water pollution, solid waste, land use, and water consumption.[173]

This novel approach to corporate impact assessment seems to be an interesting communication tool to show the BASF's commitment to the environment and society.

[167] Pieter Baert, Frederik Lange and James Watson "The Role of Taxes on Investment to Increase Jobs in the EU – An Assessment of Recent Policy Developments in the Field of Corporate Taxes", Study for the EU Economic and Social Committee (May 2019), available at: https://www.eesc.europa.eu/sites/default/files/files/qe-03-19-343-en-n.pdf, at 1.
[168] Reference made to Clemens Fuest, Andreas Peichl, Sebastian Siegloch: "The incidence of corporate taxation and its implications for tax progressivity" (2017), referred to in Baert et al ibid at 21.
[169] BASF, "We create value", available at: https://www.basf.com/global/en/who-we-are/sustainability/we-drive-sustainable-solutions/quantifying-sustainability/we-create-value.html; and BASF " BASF's Value-to-Society: Results 2013-2018 at Group level", available at: https://www.basf.com/global/en/who-we-are/sustainability/we-drive-sustainable-solutions/quantifying-sustainability/we-create-value/impact-categories.html.
[170] Ibid.
[171] Dirk Voeste and Christian Heller, "BASF'S Value-to-Society" *The Reporting Times* (May 2018) 10.
[172] "We Create Value" above n 169.
[173] Ibid.

Nevertheless, it is noted that there are limitations to measuring these impacts in monetary terms, or financially quantifying respect for human rights.

4.3 Language used to describe due diligence

Respondents were asked what language they use to describe their due diligence processes. However, it should be noted that the survey responses and interviews demonstrates that terminology differs from one user to the next: one company's "human rights due diligence" process may cover a different or wider set of issues or go deeper into the supply chain than the process which another respondent has described with a similar name. Similarly, different companies describe very similar or identical processes, roles and responsibilities using different terms.

The terminology selected by most business respondents (32.43%) and general respondents (54.10%) is "human rights due diligence". This is followed by a mix of other phrases (18.92% business, 36.61% general) related to supply chain due diligence, supplier codes of conduct or ethical sourcing. In the business survey, the third most-selected phrase was "sustainability due diligence", but only selected by a few (14.19%), and followed closely by "social, environmental and human rights due diligence" (13.51%). In the general survey, "social, environmental and human rights due diligence" was the third most-selected options, by 35.52%, before "sustainability due diligence", selected by 30.05%.

Only 1.35% of business respondents and only 6.56% of general respondents use the phrase "climate change due diligence", which was the least selected phrase in both surveys. Noting the above-mentioned responses regarding the frequency with which climate change impacts are viewed as either expressly or implicitly included in due diligence processes, this infrequent use of the phrase "climate change due diligence" predominantly suggests that self-standing processes which focus *exclusively* on climate change are rare.

Answers provided by industry organisations in optional text boxes also emphasise that "each company has its own terminology to describe due diligence processes". Areas which are commonly covered, despite the chosen language used to describe the process, include "human rights, anti-bribery, environment, climate change, social issues." It was also noted that many companies use the phrase environmental, social and governance or "ESG" due diligence.

Interviewees suggested that any regulatory mechanism should build upon the influence and strength of the due diligence concept of the UNGPs. Several references were made to the uptake which the UNGPs have had, also in terms of due diligence expectations contained in the OECD Guidelines and other mechanisms. The OECD Guidelines were frequently mentioned as an example of how the UNGPs concept of due diligence can be expanded and applied to other areas of responsible business conduct such as impacts on the environment and climate change. John Ruggie described the revised OECD Guidelines "the first [inter-governmental instrument] to take the Guiding Principles' concept of risk-based due diligence for human rights impacts and extend it to all major areas of business ethics."[174]

[174] OECD "OECD Guidelines for Multinational Enterprises: Responsible Business Conduct Matters" ("OECD RBC Guidance"), available at: http://mneguidelines.oecd.org/MNEguidelines_RBCmatters.pdf at 5.

Regarding building on the strength of the concept of due diligence which was introduced by the UNGPs and embedded in the OECD framework, an interviewee from a multinational food and drinks company indicated:

> I think the Guiding Principles were quite clear in terms of the scope that was expected from companies in terms of human rights due diligence. And this is really the starting point. And the reference should be internationally recognised human rights, based on the Universal Declaration and the two Covenants. And I think, you know, this is clear, and I think this is a plus, that there is clarity in terms of what is expected from companies, because it does actually provide a framework, a clear framework for business so they know what they need to abide by. And I think that differentiates the Guiding Principles from other standards where the definition of the scope, or the reference framework is a bit less clear. And I am sure you know that clarity, for business, is at the essence.

An interviewee from an international civil society organisation argued that the focus on the normative framework is extremely helpful for companies, and that this concept should be retained:

> [H]uman rights due diligence is a concept that is still relatively new. It took many years for people to get their heads around the fact that this is not the commercial due diligence that companies are used to, and corporate lawyers are used to, and generally the commercial world is used to. This is to do with the human rights impacts of the rights-holders.

The interviewee continued to emphasise that the strength of this framework should be built upon rather than abandoned:

> And I think it would be tremendously dangerous to now start doing away with the concept for something broader to incorporate all existing social values. And ditching that concept. I think it’s too premature. And in fact it’s not been sufficiently practised…It took a long time to convince a lot of people to start using it and it would be very dangerous in terms of normative developments to now ditch the concept.

The interviewee thereafter raised a concern which was shared by a few interviewees, namely at the suggestion of changing the language of “human rights due diligence”, which interviewees described as “clear”, to “sustainability due diligence”, a concept which they described as “vague”:

> I think not referring to human rights in due diligence risks dissipating…the focus. And we could go back to environmental and social impact assessments. Which really, if they were performed properly, they were about sustainability. And we, in our own work, when we looked at environmental and social impact assessments, the social aspect of the impact assessment really didn’t ever cover the human rights. It may have done it in a generic manner, it may have done it in a large-scale manner, but it never looked at the human rights of each individual, and for instance, the human rights of women in particular. [T]he human rights lens actually allows you to look at the differentiated impact on each individual of a particular activity or project, and I think you could end up going back to the social impact assessments by talking “sustainability”. So I think it would be dangerous.
>
> And the other thing, talking “human rights due diligence”, also forces the company performing it to look at the right normative framework. They need to look at international human rights law. So basically, again, talking about sustainability risks dissipating that message that what you need to make sure you

> respect here and abide by and use as your benchmark is international human rights standards. When it comes to children, you know, what does that look like in terms of children's rights, and women, and etcetera.

The general view of most stakeholders was that the UNGPs concept of due diligence (which has influenced the OECD Guidelines and other regulatory mechanisms) is useful insofar as it focuses on the steps which each individual company can be expected to take for its risks of external impacts. For example, one interviewee from an international trade association who works with large consumer-facing companies on their due diligence practices stated:

> [M]ost [of our brands] have adopted the UNGP approach in terms of recognizing that due diligence is about with the workers, recognizing that it is about actual avoidance of potential risks. I think most are on board with that definition, and they'll need to engage in identification of salient risks and prioritization. Then developing a strategic plan for the fine-tuned due diligence approaches.

An interviewee from a multinational food and drinks company similarly indicated that the clarity of the concept of due diligence introduced by the UNGPs has been very helpful:

> When it comes to think [about] regulation [or] legislation, for us, the focus of such legislation should be to a kind of implementation of the UN Guiding Principles. Because the framework of the Guiding Principles is already quite well understandable, but still not mandatory. And it is a bit the weakness of this framework. So when it comes to go towards mandatory due diligence, the reference should stay the UN Guiding Principles. Otherwise, you will lose companies, even those who are maybe well-advanced or leaders. Because without clarity of the intention of the legislators business cannot really operate in good conditions.

Interviewees noted that usefulness of the language of the UNGPs for introduction into a legal standard with references to the French Duty of Vigilance Law. As noted also in the Regulatory Review and the France Country Report, the background materials of the French law expressly state that the UNGPs form the frame of reference for the French law. An interviewee from a French business organisation stated that:

> We consider that the [French] law is a transposition of the UNGPs (...) We use the UNGPs to interpret this law because it is a *loi cadre* and nobody explained how to interpret the law.

Evidencing the usefulness of the UNGPs concepts for stakeholders across the spectrum, when asked how companies could improve their due diligence practices, a survey respondent from an industry organisation indicated in an optional text box:

> Sectors and companies not using/ following UN Guiding principles or similar practices need to start doing that.

Case study: Vattenfall and Limiting Environmental Damage

Vattenfall is a Swedish state-owned energy company. It produces electricity and heat, and conducts sales operations in both segments. Vattenfall's main markets are Denmark, Finland, the Netherlands, Germany, the United Kingdom, and Sweden. It provides an example of an energy company actively engaging in due diligence which also includes climate change.

In 2016, the German environmental and human rights organisation Urgewald published a report entitled "Energy You Want?: Vattenfall's Dark Side". It described Vattenfall's customer relationship to mining companies in the north of Colombia which were found to employ private armies, and to be a key source of financing for a paramilitary group which had killed over 3,100 people in the coal mining region between 1996 and 2006.[175] In addition, the report pointed out that Vattenfall still owned mines and power stations in Germany where lignite – a highly CO_2-polluting type of coal – was extracted or burnt. The report blamed the company for selling its lignite assets instead of beginning a phase-out of them.[176]

Vattenfall responded to this report with two letters, addressing its "decision to reduce its CO_2 exposure and to grow in renewables" as a "responsible seller".[177] It also pointed to its policy of not directly sourcing from Colombian companies that do not "publicly condemn any human rights violations in the past which took place in the region where they operate currently, publicly support the Colombian Peace Process and publicly support a reconciliation procedure for the victims of past human rights violations".[178]

Currently, Vattenfall's social responsibility strategy publicly asserts that the company is committed to increasing its leverage throughout its supply chain, to fostering engagement with its suppliers, and to enhancing suppliers' sustainability performance.[179] These principles are reflected in Vattenfall's Code of Conduct for Suppliers, whereby Vattenfall reserves "the right to conduct due diligence by regularly and systematically identifying and assessing human and labour rights, environment and business ethics related risks and impacts in its supply chain" in order to mitigate impacts and ensure responsible sourcing.[180] Further, the company publishes its human rights,[181] sustainability,[182] and environmental policies.[183]

Regarding the introduction of carbon reduction in its due diligence process, Vattenfall has publicly committed to reducing its CO_2 emissions by establishing a roadmap whereby it will "completely phase out coal in its heat portfolio in Germany and the Netherlands by 2030" and "become totally climate neutral in the Nordic region by 2030".[184] This appears to show a change in the company's strategy, since in the past it filed two investor-state claims under the Energy Charter Treaty against Germany's policies on restrictions of coal (2009) and on the phase-out of two nuclear plants (2012).[185] The first claim was settled

[175] Endcoal, "Energy You Want? Vattenfall's Dark Side" (April 2016), available at: https://endcoal.org/resources/energy-you-want-vattenfalls-dark-side/.
[176] Business & Human Rights Resource Centre ("BHRRC") "Vattenfall Continues to Buy Coal from Conflict Zones & Emit High CO2 Emissions despite Climate Goals" (May 2016), available at: https://www.business-humanrights.org/en/vattenfall-continues-to-buy-coal-from-conflict-zones-emit-high-co2-emissions-despite-climate-goals-company-response-provided.
[177] Annika Ramsköld, "Vattenfall's Response to Urgewald Report" (13 May 2016), available at: https://www.business-humanrights.org/sites/default/files/documents/20160513_Vattenfall%27s%20response_Business%20and%20Human%20Rights%20Centre_Urgewald%20report.pdf.
[178] Vattenfall, "Vattenfall Views on Hard Coal Sourcing from Colombia" (13 May 2016), available at: https://corporate.vattenfall.com/globalassets/corporate/sustainability/doc/statement_vattenfalls_views_on_hard_coal_sourcing_from_colombia_final_130516.pdf.
[179] Vattenfall, "Supply Chain Responsibility", available at: https://group.vattenfall.com/who-we-are/sustainability/social-responsibility/supply-chain-responsibility.
[180] Vattenfall, "Code of Conduct for Suppliers" (July 2017) available at: https://group.vattenfall.com/siteassets/corporate/who-we-are/about_us/suppliers/code_of_conduct_for_suppliers_en_.pdf at 1.5.1.
[181] Vattenfall, "Human Rights Policy" (December 2018), available at: https://group.vattenfall.com/siteassets/corporate/who-we-are/sustainability/doc/human_rights_policy_190320_v02.pdf.
[182] Vattenfall, "Sustainability Policy" (December 2018), available at: https://group.vattenfall.com/siteassets/corporate/who-we-are/sustainability/doc/sustainability_policy_2018.pdf.
[183] Vattenfall, "Vattenfall Environmental Policy" (April 2018), available at: https://group.vattenfall.com/siteassets/corporate/who-we-are/sustainability/doc/181022_environmental_policy_en.pdf.
[184] Vattenfall, "CO2 Roadmap", available at: https://group.vattenfall.com/what-we-do/roadmap-to-fossil-freedom/co2-roadmap.
[185] Corporate Europe Observatory ("CEO") and others, "Polluters' Paradise. How Investor Rights in EU Trade Deals Sabotage the Fight for Energy Transition" (2015), available at: https://corporateeurope.org/sites/default/files/pollutersparadise.pdf; Nathalie Bernasconi-Osterwalder and Rhea Tamara Hoffmann, "The German Nuclear Phase-Out Put to the Test in International Investment Arbitration? Background to the New Dispute Vattenfall v. Germany (II)", *International Institute for Sustainable Development ("IISD") Briefing Note*, (June 2012), available at: https://www.iisd.org/pdf/2012/german_nuclear_phase_out.pdf

in 2011, after Germany agreed to "water down" the environmental standards.[186] The second is still pending.[187] This provides an example of problematic duality between a company's (voluntary) corporate social responsibility commitments and its legal strategies, which, as Cees Van Dam has pointed out, is a recurring tensions within companies once they publicly commit to human rights and environmental due diligence.[188]

Following the concerns raised by Urgewald on Colombian coal suppliers, Vattenfall conducted and published the first human rights risk assessment on its Colombian coal supply chain in November 2017.[189] The report acknowledges that coal mining in Colombia had occurred in a context of violence which might have had negative impacts on many people, and, hence, "companies should take concrete efforts to engage in constructive dialogue with victims of past human rights violations".[190] The risk assessment was updated in January 2019,[191] where it was disclosed that Vattenfall removed the mining company Drummond from their list of suppliers given that the latter decided to discontinue the direct dialogue with the former's human rights risk assessment and action plan.[192]

In sum, Vattenfall provides an example of a company now committed to preventing its contribution to climate change whilst undertaking novel risk assessments to enhance due diligence along its supply chain.

4.4 Due diligence practices in own operations

Survey respondents were asked which actions companies currently take to prevent, mitigate or remedy the adverse human rights and environmental impacts of their own operations.

Business respondents indicated that the most frequently used actions are training on human rights or environmental impacts (69.01%) and contractual clauses and codes of conduct (69.01%), followed closely by audits (67.61%). Internal or external investigations were selected by 45.77%, and working with human rights and environmental experts by 40.85%. Other actions selected by business respondents include additional staff for human rights or environmental measures (35.92%) and working with local partners (35.92%).

The top most selected actions by general stakeholders about due diligence practices in companies' own operations were contractual clauses and codes of conduct (61.76%), followed by audits (60.29%).

It is noted that here, the views of stakeholders corresponded with the information provided by companies about their own due diligence practices. However, it is also noted that both these top actions, namely contractual clauses and codes of conduct, and

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at 8; Nathalie Bernasconi-Osterwalder and Martin Dietrich Brauch, "The State of Play in Vattenfall v. Germany II: Leaving the German Public in the Dark" *IISD Briefing note* (December 2014), available at: https://www.iisd.org/library/state-play-vattenfall-v-germany-ii-leaving-german-public-dark at 8.

[186] Bernasconi-Osterwalder and Hoffmann ibid at 3.

[187] *Vattenfall AB and Others v. Federal Republic of Germany* ICSID Case No. ARB/12/12, available at: https://icsid.worldbank.org/en/Pages/cases/casedetail.aspx?CaseNo=ARB/12/12.

[188] Cees Van Dam, *Enhancing Human Rights Protection: A Company Lawyer's Business*, Rotterdam School of Management, Erasmus University (2015) at 37.

[189] Vattenfall, "A Human Rights Risk Assessment in Colombia: Vattenfall's Efforts on Coal Supply Chain Responsibility" (2017, available at: https://www.business-humanrights.org/sites/default/files/documents/vattenfall_coal_sorcing_report_2017_0.pdf.

[190] Ibid at 82.

[191] Vattenfall, "Vattenfall's Efforts on Coal Supply Chain Responsibility: Human Rights Risk Assessment in Colombia – Update January 2019" (2019), available at: https://group.vattenfall.com/siteassets/corporate/who-we-are/sustainability/doc/vattenfall_hardcoalsourcingfromcolombia-updatejan2019.pdf.

[192] Ibid at 4.

audits, respectively, relate to an oversight of the impacts of third parties such as suppliers, and were indeed again selected as the top two actions for due diligence in the upstream and downstream supply chain below.

The third selected action by general stakeholders relating to due diligence in companies' own operations was training on human rights and environmental impacts (53.43%), which was not one of the top selected actions by business stakeholders relating to their due diligence for own operations.

An interviewee with expertise on business and human rights in Germany indicated that, due to differences in risks and exposures to date, due diligence practices are more developed in certain sectors than others:

> [I]n the textile or garment sector there is increasing experience of companies, not only big ones but also medium sized companies, who have started to have comprehensive human rights due diligence processes. This is of course due to high exposure of this sector to public scrutiny following well-known catastrophes in production countries. The more structured, systematic approach of the garment sector is also due to a government reaction, with the Alliance for sustainable textile, which is a sectoral multi-stakeholder initiative. This initiative has already introduced a concept of human rights due diligence to the garment sector in Germany in a rather broad way.
>
> In other sectors, systematic human rights due diligence apparently is still not the majority practice. For example in machine engineering, which is one of the leading and most globalised sectors of German industry, but at the same time very strongly characterised by SMEs. We hear that there is so far very limited best practice examples of systematic human rights due diligence.

UNGP 19 indicates that effective integration of due diligence includes the allocation of resources, and requires that "[r]esponsibility for addressing such impacts is assigned to the appropriate level and function within the business enterprise", as well as "[i]nternal decision-making, budget allocations and oversight processes enable effective responses to such impacts."

An interviewee who works with consumer-facing brands on their due diligence practices indicated:

> The majority of [our] companies, I think, they do take this seriously, they're engaging in due diligence but they're also not dedicating sufficient resources.

The concept of due diligence is based on the acknowledgment that companies do not have unlimited resources and may prioritise those impacts that are the most "severe" (defined by the UNGPs and the OECD Guidelines),[193] the "most significant",[194] or the most "salient" (terminology used by the UNGPs Reporting Framework).[195] One survey respondents indicated in an optional text box, when asked in which way current due diligence practices falls short:

> Mainly the need to prioritise, based on salient impacts, rather than tackle everything at the same time.

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[193] UNGP 17(b).
[194] OECD Guidelines for Multinational Enterprises, 2011, Chapter II, Commentary, paragraph 16: "Where enterprises have large numbers of suppliers, they are encouraged to identify general areas where the risk of adverse impacts is most significant and, based on this risk assessment, prioritise suppliers for due diligence."
[195] Shift and Mazars, "The UN Guiding Principles Reporting Framework", available at: https://www.ungpreporting.org/.

However, it was emphasized that prioritization should only take place after all actual or potential issues have been identified and assessed. One interviewee from a multinational company described this process as follows:

> The OECD guidelines say you need to review all the risks and you need to include the full portfolio of negative impacts. So there is no question about being selective. You are selective once you have made your risk analysis, in terms of where you're going to focus your in-depth due diligence, where to mobilise resources to mitigate the risk. The issue starts when you've got an NGO that is particularly interested in the development of specific rights, for example women's rights in a particular country. And they say you should also focus on women's rights. But we say that our assessment shows that we have more severe risks of, say, child labour. So we are not going to spend our limited resources on that other risk. That is one big debate.

The concern raised by this interviewee also applies to the question of issue-specific regulation, discussed below.

4.5 Due diligence practices in supply and value chains

Upstream supply chain

Survey respondents were asked whether current due diligence practices include the human rights or environmental impacts of third parties in the supply chain or value chain. The value chain was defined as "the upstream and downstream life cycle of a product, process, or service, including material sourcing, production, consumption, and disposal/recycling."

In the business survey, the majority (51.82%) of respondents who undertake due diligence indicated that third party impacts are included for first tier suppliers only. Of the remaining respondents who undertake due diligence, 16.06% indicated that their due diligence includes the impacts of the entire upstream supply chain, beyond the first tier, and 16.06% indicated that they include the impacts of the entire value chain, both upstream and downstream. Of those companies that undertake due diligence, 6.57% indicated that the impacts of third parties are not included.

An interviewee from a large multinational company indicated:

> It is true that we are putting a lot more efforts in subsidiaries that we control and entities with whom we have direct relationships. This is of course easier and that is where we put our stronger efforts. ... For instance ... we have committed to an obligation of result in relation to our controlled subsidiaries to respect and embed the core ILO Conventions and other international standards, and to do our best efforts to promote these principles in the non-controlled subsidiaries and along the supply chain.

The interviewee added:

> When we have control it is easier [...] However when we don't have control [with second tier suppliers, and so on] we are expecting the first tier suppliers who are having the relationship with their own counterparts to do the same [implement human rights commitments]. We are not ourselves directly controlling but we are expecting those people to control.

Survey respondents were asked to indicate which actions companies currently take to prevent, mitigate or remedy the adverse human rights and environmental impacts of third parties in their upstream and downstream value chains.

“Upstream” activities were defined as including “operations that relate to the initial stages of producing a good or service, including material sourcing, material processing, and supplier activities”. "Downstream" activities were defined as including “operations that relate to processing the materials into a finished product and delivering it to the end user, including transportation, distribution, consumption and disposal/recycling.” We asked investor companies to answer questions about suppliers with respect to investee companies, where possible.

For business and general respondents alike, contractual clauses and codes of conduct were the most frequently selected actions in both upstream and downstream value chains. This was followed by audits as the second most frequently used action in both the upstream and downstream value chain, similarly selected as such by both business and general respondents.

Further activities used in the upstream supply chain include, in order of selection, engagement or leverage with suppliers, and training on human rights and environmental impacts. Business respondents selected termination of relationships for non-compliance with standards as the fifth most frequently used due diligence action in the upstream supply chain, whereas general stakeholders selected working with local partners.

An interviewee who advises companies on their due diligence practices highlighted that one of the common shortcomings of contractual clauses are that they are not being monitored or implemented:[196]

> We need a way to check, because the only thing now is that companies say: ‘Yes, we have clauses’. But so far they haven’t been checking their implementation. We are currently working on this, to encourage them to check and monitor.

Another interviewee who works with companies on their due diligence practices, described the following common practices:

> In terms of upstream, a range of different practices, social auditing is still extremely popular and relied on. You might be familiar with Sedex as perhaps the largest and most recognizable of the big brands.
>
> Other companies have actually moved away from social auditing and have in-country staff. Some big brands try not to use external auditors but rather send company reps to factories to inspect individually and to both provide feedback and to try and support their companies in proven practices.
>
> A lot of our companies use private consultancies to guide their due diligence work both in terms of the desk research, but also in-country, visiting workplaces, conducting impact assessments, conducting risk analysis. That is also quite common, and particularly with the larger corporations.

For the purposes of mapping risks in their supply chains, the interviewee described the process which many companies use:

> We know that a lot of companies engage in more salient risk mapping and prioritization exercises to help them direct resources appropriately. A lot of them use quite a rudimentary traffic-light system whereby they'll have a fairly basic metric. Whereby there's a series of non-compliant [factors] that are considered very serious. That might indicate that the supplier is given an orange or red light

[196] See also McCorquodale et al above above n 143.

> and requires follow up, whereby the auditor checks why this has not raised any serious concerns. They use that to rate individual suppliers to guide their work.

An interviewee from a financial institution described how due diligence works in the banking sector:

> As a bank we expect our clients to do due diligence as well. So the due diligence that banks do is always sort of second tier due diligence. Our clients are primarily responsible to work in their supply chains on their challenges. And we check whether our clients are doing that in a good way. And we have an idea about what standards in a sector should look like, but in the end it's our clients that should actually do that. We may have clients that are really not interested in human rights or have quite weak policies or procedures in place or do not have adequate staff or capacity to do so. So for some clients [an EU level regulation on due diligence in supply chains] may level the playing field, and our role as a bank in checking whether our clients are up to speed may be eased by a mandatory framework that applies to all clients.

Downstream value chain

For business and general respondents alike, contractual clauses and codes of conduct were the most frequently selected actions in both upstream and downstream value chains, followed by audits.

For the downstream value chain, the third most selected action by both business and general survey respondents was working with human rights and environmental experts. Business respondents followed this with training on human rights and environmental impacts, engagement or leverage with other third parties (presumably downstream in the value chain) and additional staff for human rights or environmental measures. General stakeholders selected similar actions but in a slightly different order.

Regarding the downstream value chain, an interviewee from a multinational food and drinks company indicated:

> From a legislative perspective, I would say that the way the legislation should be shaped, should most probably address first the upstream supply chain, if it has to be differentiated, because this is where all businesses who decided to do something began with, and this is also what, in my view, [aligns with] the expectations of the civil society and the regulators.

Divestment was the least selected due diligence action by both business and general respondents in both the upstream and downstream supply chain.

Case study: Lundbeck and Akorn: Restricting pentobarbital for lethal injections in the US

An example of how a company can introduce changes to address their involvement in human rights violations in their downstream supply chain are provided by the case study of Lundbeck and Akorn.

Lundbeck, a Danish pharmaceutical company, manufactured pentobarbital under the name of Nembutal, which is licensed for refractory forms of epilepsy and for usage as an anaesthetic. The company was the only licensed supplier in the US in 2011. Early that year it was discovered that the US' authorities had begun to use Lundbeck's pentobarbital for the purposes of lethal injections.[197] Reprieve and Amnesty International denounced the situation and appealed to Lundbeck to put an end to the use of the drug in executions.[198]

In this context, if the company withdrew its drug from the market it could affect the right to access to medicine, including for some which use the drug against life-threatening epilepsy. On the other hand, if its product continued to be used for lethal injections, the company risked being accomplice to violating the right to life.[199]

Facing this dilemma, Lundbeck showed in a letter its opposition of the use of Nembutal for execution purposes and urged this use to be discontinued. Yet, it argued that the way in which its product was used by licensed health care professionals was beyond the company's control.[200] In June 2011, a group of clinicians published an open letter in *The Lancet* (a respected medical journal) criticising the company and claimed that it "should restrict the distribution of pentobarbital to legitimate users", as it was doing with some other of its neurological products in the US.[201]

On 1 July 2011, Lundbeck announced that Nembutal would be exclusively supplied "through a specialty pharmacy drop ship program that will deny distribution of the product to prisons…carrying out the death penalty by lethal injection".[202] In doing so, the company guaranteed supplies of the product only to hospitals and therapeutic centres for its indicated use,[203] and it obliged purchasers to:"[S]ign a form stating that the purchase of Nembutal is for its own use and that it will not redistribute any purchased product without express written authorization from Lundbeck. By signing the form, the purchaser agree[d] that the product will not be made available for use in capital punishment".[204] This was a novel practice amongst pharmaceutical companies.[205]

In December 2011, Lundbeck sold Nembutal to Akorn.[206] Lundbeck explained that its decision was based upon economic considerations and was unrelated to the issue of pentobarbital having been used in lethal injections.[207] Currently, pentobarbital is manufactured by Akorn and two other companies, and control systems seem to be in place to prevent the drug from being used in lethal injections.[208] In 2015, Akorn adopted

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[197] Karin Buhmann, "Damned If You Do, Damned If You Don't? The Lundbeck Case of Pentobarbital, the Guiding Principles on Business and Human Rights, and Competing Human Rights Responsibilities" (2012) 40 *The Journal of Law, Medicine & Ethics* 206 at 206.
[198] Reprieve, "Reprieve Calls on Danish Pharmaceutical Company Lundbeck to Take Decisive Action as Mississippi Becomes the Fourth State to Seek Its Pentobarbital to Kill" (24 March 2011), available at: https://reprieve.org.uk/press/2011_03_24mississippi_pentobarbital_lundbeck; Amnesty International USA "Denmark Company Supplies Major U.S. Executioners" (30 March 2011), available at: https://www.amnestyusa.org/denmark-company-supplies-major-u-s-executioners.
[199] Buhmann above n 197 at 206.
[200] "Letter Pentobarbital Manufacturer Sent to DOC's about Using Pentobarbital for Executions" (26 January 2011), available at: https://deathpenaltyinfo.org/documents/LundbeckLethInj.pdf.
[201] Ulf Wiinberg, "Open Letter to Ulf Wiinberg, Chief Executive of Lundbeck Pharmaceuticals – Response from Lundbeck" (2011) 377 *The Lancet* 2079.
[202] Lundbeck "Lundbeck Overhauls Pentobarbital Distribution Program to Restrict Misuse" (1 July 2011), available at: https://investor.lundbeck.com/news-releases/news-release-details/lundbeck-overhauls-pentobarbital-distribution-program-restrict.
[203] Reprieve, "Factsheet on Lundbeck's Nembutal", available at: https://reprieve.org.uk/wp-content/uploads/2014/10/2011_11_01_PUB_Lundbeck_distribution_system.pdf at 5.
[204] Lundbeck above n 202.
[205] Ty Alper, "The United States Execution Drug Shortage: A Consequence of Our Values" (2014) XXI *The Brown Journal of World Affairs* 27 at 31.
[206] Akorn "Akorn Acquires Three Hospital-Based Branded Injectables from Lundbeck", 22 December 2011, available at: http://investors.akorn.com/news-releases/news-release-details/akorn-acquires-three-hospital-based-branded-injectables-lundbeck.
[207] Anita M Halvorssen and Karin Buhmann, "Extraterritorial Regulation of Companies and the UN Guiding Principles on Human Rights and Business" in Manoj Kumar Sinha (ed), *Business and Human Rights*, SAGE Law (2013) 152.
[208] Lethal Information Center, "Controlled Medicines", available at: https://lethalinjectioninfo.org/controlled-medicines/.

a policy to prohibit the direct sales of pentobarbital to prisons, and to restrict the sales to a group of wholesalers who agree to keep the drug out of correctional institutions.[209] According to Akorn, the availability of Nembutal to secondary customers or correctional institutions is blocked either by agreement with the hospital customers known by Akorn, or by contract with their distributors, which act as drop-shipping agents.[210]

Moreover, the Lethal Injection Information Center, an initiative of the NGO Reprieve, publishes a list of controlled medicines for which distribution controls are in place to ensure that products are being sold exclusively for legitimate medical use.[211] This seems to suggest that the attention which Lundbeck attracted incentivised the pharmaceutical industry to take actions in their downstream supply chains for their negative human rights impacts to be addressed.

The Lundbeck and Akorn examples demonstrate how companies can take actions to address their human rights impacts in a tailored way, even in the downstream value chain, which is notoriously hard to monitor. It is, however, noted that, in the absence of legal requirements, these changes were predominantly driven by the pressure received from civil society and clinicians.

In relation to downstream due diligence, the US Department of State recently issued a Draft Guidance for the export of hardware and technology with surveillance capabilities and/or parts/know-how.[212] The guidance indicates that such items:

> [C]an be misused to violate or abuse human rights when exported to government end-users or private end-users that have close relationships with the government. In some cases, governments have misused these items to subject entire populations to arbitrary or unlawful surveillance, violating the right to privacy as set out in the Universal Declaration of Human Rights (UDHR) and the International Covenant on Civil and Political Rights (ICCPR).
>
> In other cases, governments employ these items as part of a broader state apparatus of oppression that violates human rights and fundamental freedoms enumerated in the UDHR and ICCPR, including freedoms of expression, religion or belief, association and peaceful assembly.
>
> The misuse of an item can take many forms, including to stifle dissent; harass human rights defenders; intimidate minority communities; discourage whistle-blowers; chill free expression; target political opponents, journalists, and lawyers; or interfere arbitrarily or unlawfully with privacy. Arbitrary or unlawful interference with privacy is a particular concern in this context, especially since such interference may also impede the enjoyment of other human rights, such as the rights to freedom of expression, to hold opinions without interference, and to freedom of association and peaceful assembly. These and other rights are among the foundations of any democratic society.

[209] Akorn, "Akorn Adopts Comprehensive Policy to Support the Use of Its Products to Promote Human Health", 4 March 2015, available at: http://investors.akorn.com/news-releases/news-release-details/akorn-adopts-comprehensive-policy-support-use-its-products.
[210] Dewey Steadman, "Taking a Stand to Promote Human Wellness" UKSIF Death Row Pharma webinar, 24 September 2015, available at: http://uksif.org/wp-content/uploads/2015/10/UKSIF-Death-Row-Pharma-webinar-slides.pdf at 19.
[211] "Controlled Medicines" above n 208.
[212] U.S. Department of State, "Draft U.S. Government Guidance for Export of Hardware, Software and Technology with Surveillance Capabilities and/or Parts/Know-How", available at: https://www.state.gov/wp-content/uploads/2019/09/DRAFT-GUIDANCE-FOR-THE-EXPORT-OF-HARDWARE-SOFTWARE-AND-TECHNOLOGY-WITH-SURVEILLANCE-CAPABILITIES.pdf.

The guidelines seek to "provide insight to exporters on considerations to weigh prior to exporting these items" and assist them with the implementation of the UNGPs and OECD Guidelines for Multinational Enterprises.

4.6 Traceability and the scope of the supply chain

Due to the complex, dynamic and non-transparent nature of global supply chains, traceability is a major challenge for companies aiming to undertake supply chain due diligence. An interviewee from the European Confederation of Directors Institutes ("EcoDa"), an organisation which represents 22 national institutes of directors in Europe, indicated:

> [I]n the real world most companies have a large amount of different supply chains - in major multinational corporations often to be counted in hundreds - many of them extremely complex, spanning over a variety of different sorts of suppliers and subcontractors as well as across national and inter-continental borders over the entire world.

This problem is aggravated by the use of complex corporate structures consisting of various separate legal entities in different legal jurisdictions. These problems are discussed further in the Problem Analysis and Regulatory Review section.

Beate Sjåfjell, who leads the SMART Project, explained these problems in an interview as follows:

> [C]orporate law in itself gives businesses a vast opportunity to fragment their business across a number of legal entities through corporate groups. And then in addition, with financial engineering, it is possible to have control of a company without officially being a parent company. So the problem that is already there in company law, that a parent company can control a subsidiary in another country and get profits from that and not be responsible in most cases if something goes wrong in that subsidiary or the community where the subsidiary is. That is then even more exacerbated through the possibility, through financial engineering, of control that is not visible from a company law perspective. That's a second thing.
>
> And then a third thing, which exacerbates this even further, is the shift from corporate governance to governance through contract, so with the supply chains. Where even if somebody in a business today wakes up and thinks: 'Oh, I want to have a sustainable supply chain', then they would probably not even know what their supply chain is. They might know the first level and the second. But this is a huge problem.

A survey respondent from an industry organisation working in the cocoa sector describes some of the common challenges which companies experience in their supply due diligence, regarding complexity, and a lack of transparency:

> Many commodities such as cocoa, are produced by millions of smallholder farmers. Sourcing from hundreds, even thousands of different farmers, each of them with their own characteristics and from different geographical areas, can make the process of fully mapping the cocoa supply chain a challenging task, even for sophisticated upstream companies. In addition, the cocoa supply chain is complex, with many intermediaries involved. Such third parties may not have enough visibility or knowledge on where the product is coming from or may not be incentivized to share such information with upstream companies.

However, another interviewee from an environmental NGO argued that traceability is less of a practical hurdle than is often thought:

> A lot of people talk about the problem that it's too difficult to trace the supply chain. But from speaking to several companies, they've told me sort of privately that this is just a bogus argument. Because they already trace their full supply chain for food safety and for quality. So it is perfectly possible to do it. The reason that they don't do it for deforestation and human rights issues is that it's expensive to do in any case. And they're not going to put all that money unless their competitors also have to do it as well. ... Often traceability is framed as a technical problem, but according to what these companies told me it's technically fully possible, it's just that it cost money. And no-one is going to send that money on a voluntary basis if their competitors aren't going to do that as well.

One multinational garment sector interviewee indicated:

> We do have a dedicated team which are just for traceability. They are textile engineers so they have different systems to make sure that the factories that you are declaring are actually the only factories that you are using…We [now] have the technical expertise to analyse the capacity of the factories that the supplier is declaring, making sure, crossing those figures with the number of garments that they were supposed to be making in a specific period of time, and counting actually the minutes that you spend per each garment, and then doing specific audits to make sure that this production is actually being done there. Everything becomes more and more sophisticated. So you can control, and you have your supply chain is visible. And once you have all the cards on the table it's easier to understand.

The interviewee added:

> We also have partnership with the ILO, in particular working with, because we want to work beyond all the tiers that we have identified so far. So we have a PPP with the ILO for cotton. So we want to go now to the cotton fields, which is something that is unexplored for us. And the traceability, it's a completely different world.

Case study: Marks & Spencer and mapping supply chains

Marks & Spencer (M&S) is a British supermarket chain which retails both apparel and agricultural products. M&S's management of its supply chain provides a good example of mapping a worldwide network of suppliers.

In a written evidence submitted to the Joint Committee on Human Rights of the British Parliament during 2016, M&S highlighted the efforts which the company has taken to communicate its commitment to human rights. It expressed its support for the momentum created by the British Government via the UK National Action Plan on Business and Human Rights, the UK Modern Slavery Act, the UK government's funding contribution for the Corporate Human Rights benchmark, the extended investigatory remit of the Gangmasters Licensing Authority, and the creation of a new Labour Market Enforcement Director.[213] M&S also encouraged the UK Government "to continue its role in influencing international governments" on human rights issues with similar measures.[214]

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[213] Marks & Spencer, "Written Evidence from Marks & Spencer (HRB0013)" (July 2016) in UK Joint Committee on Human Rights, *Human Rights and Business 2017: Promoting responsibility and ensuring accountability*, available at: http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/human-rights-committee/human-rights-and-business/written/34910.html.
[214] Ibid.

In terms of M&S's practices for due diligence, of particular interest is the company's interactive map of its sourcing locations.[215] This map shows the type of product manufactured and the address, as well as the male/female ratio, the exact number of workers and whether trade unions or workers committees are in place. The map follows M&S's commitment to publish an annual list of their clothing manufacturers. The factories appearing in the map are directly contracted by M&S direct suppliers "to produce finished goods which are ready for retail and bear M&S brand logos and marks".[216] The data contained in the map is sourced on self-declared information by the suppliers and the database Supplier Ethical Data Exchange, which is then reviewed by M&S Regional Office teams.[217]

However, the mapping only includes suppliers with which the company has a direct relationship, and therefore excludes factories beyond the first tier of their supply chain.[218] The map also excludes small European meat and artisanal cheese suppliers[219] Following pressure by the campaign "Who picked my tea?", led by Traidcraft Exchange, M&S added coffee and tea to its sourcing map in March 2019,[220] and publicised it through its blog.[221]

M&S was highest-ranked agricultural products company in the Corporate Human Rights Benchmark in 2018,[222] and second highest in 2019.[223] It also topped a list ranking British companies' efforts in tackling modern slavery in 2018.[224]

M&S provides an example of a company which has been able to trace and publicise details about its direct supply chain, including in sectors such as garment and agriculture which are notorious for the complexity of supply chains. This transparency effort is accompanied by an active communication policy, which fosters dialogue between competitors and promotes accountability in their sector.

Case study: Hennes & Mauritz and transparency in the supply chain

Hennes & Mauritz (H&M) is a Swedish company manufacturing and distributing apparel worldwide. Its case provides an innovative example of transparency along their supply chain. On 23 April 2019, H&M announced that they will be providing information about the supplier of every piece of garment, becoming the first major retailer to do so. This effort enhances their novel approach of grading their suppliers, whereby each of its first-tier suppliers are graded into platinum, gold, silver or other.[225]

H&M's customers can now know where each clothing sold by the company was produced

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[215] Marks & Spencer, "Interactive Supply Chain Map", available at: https://interactivemap.marksandspencer.com/.
[216] Ibid, "Find out more".
[217] Ibid.
[218] Ibid.
[219] Ibid.
[220] Amber Milne, "M&S Reveals Tea Suppliers to Address Worker Abuse Concerns" *Thomson Reuters Foundation* (5 March 2019), available at: http://news.trust.org/item/20190305192737-12tad/.
[221] Hazel Culley, "A Transparent Cuppa – Mapping Our Tea and Coffee Supply Chains" Marks & Spencer, available at: http://corporate.marksandspencer.com/stories/blog/a-transparent-cuppa-mapping-our-tea-and-coffee-supply-chains.
[222] Corporate Human Rights Benchmark "View Banding Table" (2018), available at: https://www.corporatebenchmark.org/home.
[223] Corporate Human Rights Benchmark 2019, Key Findings Report, available at: https://www.corporatebenchmark.org/sites/default/files/2019-11/CHRB2019KeyFindingsReport.pdf
[224] Kieran Guilbert, "Marks & Spencer tops list of major British firms tackling modern slavery" *Reuters* (23 October 2018), available at: https://uk.reuters.com/article/britain-business-slavery-idUKL8N1X32M5.
[225] Sarah Ditty, "Fashion Transparency Index 2019", Fashion Revolution (2019) 53, available at: https://issuu.com/fashionrevolution/docs/fashion_transparency_index_2019/1. H&M's "gold" and "platinum" suppliers are the company's preferred and strategic partners. They profit from long-term relationships and are incentivised with joint capacity planning. Suppliers graded with "silver" have close relationships oriented to the long term. Finally "other" suppliers are producers which have been working with H&M for a period shorter than a year or that have been placed a test order. See, H&M "Supplier List", available at: https://sustainability.hm.com/en/sustainability/downloads-resources/resources/supplier-list.html.

by simply checking the website or phone app. This information is displayed next to each garment, and includes the country of production, the supplier and factory names and addresses, as well as the number workers in the factory. This step has been praised by workers' rights groups on the basis that the information available could be used by human rights organisations to monitor companies' supply chain and foster accountability.

Nevertheless, without further particulars about the human rights and environmental conditions under which suppliers operate, information about the factual details of suppliers may not be sufficient for customers to make informed choices. For this reason, Anna Bryher of Labour Behind the Label suggested that the company could consider "adding information… about wages paid at suppliers and comparing that to the living wage benchmarks or their promises on living wages".[226]

In any event, the new transparency policy of H&M is an example of how a company with a complex supply chain can achieve traceability.

4.7 Audits

As indicated above, audits is one of the most frequently used steps in existing due diligence processes, although various studies have underlined the shortcomings of audits for the purposes of effective supply chain due diligence.

One interviewee indicated how auditing would commonly be used within the due diligence process for a large supply chain:

> We have 1800 direct suppliers, what everyone calls tiers one, because we do not separate tiers…for us it's the same. And then tier two to the end of the line, we have around 7300 or 7400 per year. We train them, and the first thing that we do is that when they introduce the factories in the system we go and audit the factories before they can start working with us, to make sure that they comply with our code of conduct which is based on international standards and human rights. This audit, which is called the pre-assessment, is actually working as a first filter, to make sure that only those factories that respect human rights can be part of the supply chain. Then around that we have a number of [practices]. For example if our supplier introduces a number of factories and they do not pass the pre-assessment because they do not comply with our code of conduct, then we will work directly with the supplier to understand what is going on in their own management systems regarding sustainability or regarding human rights. So we will go and try to improve and understand why the supplier is failing in the factories that they are giving us. So even if the factories go through and the factories comply and they enter into our system, then they become part of this never-ending wheel of different assessments, not only audits.

However, a number of interviewees also pointed out the limitations of audits. One interviewee from a financial institution affirmed that:

> We all know that auditing isn't working….If you do audits on your subcontractors, we know that it's not working because it's announced, subcontractors feel pressured. What helps is that if a big company is treating the subcontractors differently, more as partners, teaching them, leaning into their problems, talking to them, engaging with them.

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[226] Sonia Elks, "Fashion Giant H&M Lists Suppliers for All Garments to Tackle Worker Abuses" *Thomson Reuters Foundation*, 24 April 2019, available at: http://news.trust.org/item/20190424114703-zfxmp.

Another interviewee working for a civil society organisation indicated:

> They [companies] commission an audit and they get the audit results and it's passed with a certain grade and that's it. They do not make further queries or question the quality or methodology of the audit. We of course often come across labour rights issues in audited factories. It's common knowledge that audits and certification schemes have their own limitations and challenges.

One interviewee working within the government of a large Member State indicated:

> There is apparently growing awareness that auditing systems often have considerable flaws, especially when it comes to social and labour standards. There is a growing feeling that in order to professionalise [due diligence] approaches, we also have to find a way how to professionalise and also streamline the global auditing systems.

One interviewee from civil society stated:

> I feel like there are some companies that do this much more thoroughly and put much more resources in it. But I would say the standard practice has been and still is to do social auditing, to allegedly control the respect for their own codes of conduct or their HR policy, which in my opinion is hugely problematic...
>
> It's a bold statement but I would say 90% of all social auditing reports are false. They either write down lies or the report may not be deliberately lying but such reports are not able to capture the reality of human rights violations on the ground, already for methodological shortcomings.

An interviewee who works with businesses in the implementation of the UNGPs explained:

> We still do see companies stuck between audits, and the idea that many leading companies know that they need to go beyond audit. But when it comes to the supply chain and overwhelming numbers, they just don't know how to reconcile what audit gives you, which is safety, and what the UNGPs and the focus on severe impacts is telling you which is: 'You're going to have to make some difficult choices if you really want to go after to the very critical issues'. And that just makes them deeply uncomfortable because they prefer things that are scalable. And inherently, when you're talking about your own operations, I mean some business will have large numbers of direct employees, they'll have large number of staff, but that's nothing in comparison to the size of their supply chain. There is just this challenge of scale. And a sense of: 'We have to have a global approach for everything, and that's how we reassure ourselves and our boards and the market though our disclosure that we have this under control'. That is inherently in tension with saying 'but how are you going to devote meaningful resources to going after some of the most severe issues?'. And I think that they are still stuck in that paradigm.

4.8 Leverage and the ability of individual companies

Survey respondents and interviewees made frequent reference to the concept of leverage, which is a key concept introduced by the UNGPs in relation to the exercise of due diligence.

The UNGPs state that companies should exercise leverage to mitigate any adverse human rights impacts that it may be contributing to. Leverage is defined as "the ability to effect change in the wrongful practices of an entity that causes a harm".[227] Where a company has leverage, it should exercise it, and where it lacks leverage, it should make efforts to increase its leverage, including through "capacity-building or other incentives".[228]

In addition, the UNGPs are clear that divestment or termination of business relationships should not be the first reaction when an adverse human rights impact is identified. Instead, a company should carefully consider the human rights impacts of terminating such a relationship:[229]

> There are situations in which the enterprise lacks the leverage to prevent or mitigate adverse impacts and is unable to increase its leverage. Here, the enterprise should consider ending the relationship, taking into account credible assessments of potential adverse human rights impacts of doing so…
>
> In any case, for as long as the abuse continues and the enterprise remains in the relationship, it should be able to demonstrate its own ongoing efforts to mitigate the impact and be prepared to accept any consequences – reputational, financial or legal – of the continuing connection.

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This approach was also reflected in the survey responses, insofar as divestment was the least selected due diligence action by both business and general respondents in both the upstream and downstream supply chain.

One interviewee from a financial institution stated that:

> Many of the NGOs that we talk to often say that we should disengage and end a relationship. It's actually much more interesting to engage with, in our case, clients, in the case of many companies, suppliers, and together identify root causes, what is going on, and work on improvements.

An interviewee from a large multinational corporation indicated:

> When you have found out that there are some issues, for instance in terms of labour rights or other issues, very often procurement people … don't want to take any risk and they just want to end the contract. It is not necessarily the right thing to do from an ethical point of view, because very often it could put the workers in a worst situation. So we are working, on a case-by-case mode [...] on remediation action plans to see if they have the capacity and the will to improve in order to avoid if possible immediate termination that would put the workers in a very bad situation.

The importance of continuous engagement for leverage with suppliers was confirmed in interviews. One interviewee from a multinational garment company indicated:

> It's been 18 years [that we have been developing our due diligence]. We have a dedicated team of 80 people, and a lot of support from the company. It's been and it still is an extremely long process. We have to keep up with the risks of the supply chain. Having people on the ground in those places where we are producing is crucial. Having good relationships with the first tier suppliers, and making them understand how the responsibility is a shared responsibility. And

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[227] Commentary to UNGP 19.
[228] Ibid.
[229] Ibid.

> providing them with the tools, because we are bigger than them and we just have more resources. So we have been making their lives as easy as possible in providing them the tools, the knowledge, the expertise that they need, to make sure that they took care of their own supply chain, with the final responsibility being ours.

An interviewee working within the government of a large Member State indicated:

> For sure, engagement for suppliers only holds true for tier 1. There is an understanding that tier 1 engagement is adequate, doable, however effective engagement with suppliers beyond tier 1 is pretty impossible. Companies report impossibility to engage with tier 2 or tier 3 because of the lack of transparency of supply chains. Large companies say it would be very helpful if there were better rules on supply chain transparency, which would allow a company not only to ask suppliers to be transparent of tier 2 or 3, but that they actually would have a legal entitlement to get this information for the sake of [due diligence].

However, companies operate in and source from host states where there are often systemic issues affecting the operating context. Survey respondents and interviewees emphasized that any legal standard should take into account that there is often only so much a single company can achieve through its own leverage when facing a systemic challenge. A survey respondent from an industry organisation indicated:

> [T]he burden of a commitment of results should not be, considering the role and shared responsibilities of (local) authorities, solely on business' shoulders.

A survey respondent from a large industry organisation indicated in optional text boxes that some of the biggest challenges their company members face in exercising due diligence include a lack of leverage:

> Some suppliers are much 'bigger' than their customers, even if those are multinational companies. Suppliers may refuse to cooperate, to respond to investigations or audit requests. In these cases, customers try to exercise leverage by dialogue and cross-sector initiatives, but it must be underlined that even large companies do not necessarily have leverage on their larger suppliers operating in third countries, which are not as concerned as themselves about reducing negative impacts.
>
> Some suppliers are in a situation of monopoly and refuse to change their practices. They know that their customers will still need to buy their products.

This was confirmed by a garment sector interviewee, who indicated that in cases where they are not the only customer of a specific factory, their leverage is often limited:

> Our approach is: let's create tools for the workers to understand and to fight for their own rights, because there is only so much that we can do to change the factory from the outside. Sometimes we are just one of the customers.

Another interviewee from an international trade association which advises companies on their due diligence explained that the inaction of others in the industry hampers the effectiveness of others' due diligence efforts:

> A lot of the due diligence we are witnessing is not really effective. It doesn't generate the data required to genuinely measure effectiveness for one thing, so it is very difficult to measure concrete impact. In terms of the cause or correlation of a company taking a specific step and engaging in a project…if there's a change

on the ground. [M]ost companies [are] simply unable to determine whether there was a direct cause or correlation to change using working conditions.

In that sense, [due diligence] is falling far short on the other side, as the working conditions in global supply chains on the whole remain very poor. We know that wages are still extremely low in sourcing destinations. Even in tier one factories in Bangladesh, where [brands have] their direct commercial leverage and a commercial relationship and a contract, wages [are] still very low [and] conditions still very poor.

That demonstrates the due diligence work is ineffective. Because some brands are taking this seriously. They are dedicating resources. They have a very talented pool of individuals experienced, passionate staff who are working on issues. And yet they can't affect change because of the wider externalities and conditions and issues in sourcing countries.

As will be seen below, some interviewees argued that mandatory due diligence regulation that applies across the board to all companies is likely to alleviate the pressure that is currently placed on individual companies, through improving corporate practices as a whole, and consequently, conditions on the ground.

Case study: Fairphone and transparency in communications

Fairphone is an Amsterdam-based social enterprise.[230] It started in 2010 as a campaign to raise awareness about conflict minerals in consumer electronics, and in 2013 was officially established as a smartphone company. To date, Fairphone has produced two smartphone models. Since the very beginning, the company attracted the attention of the media for their novel aim: to create a conflict mineral-free phone.[231]

Fairphone has shown an unusually communicative approach in the sourcing and manufacturing of their smartphones. The company has not only engaged in dialogue with their current and potential customers, but also with their competitors. Indeed, Fairphone views their products as a means to communicate: "[I]t is a vehicle for engaging stakeholders to spread a message of responsibility on the part of both producers and users, across four areas: mining, design, manufacturing and lifecycle".[232]

Fairphone has published the details of the cost of production of their two smartphone models,[233] a source map of their second terminal, [234] and an explanation of the main minerals in their smartphones and details of their global mined production.[235] This exercise of transparency is aimed at raising public awareness amongst consumers and competitors.

Fairphone has also engaged in communication with NGO stakeholders. A report by

[230] Fairphone BV, registration number KvK: 55901964.
[231] Rich McEachran, "Could Fairphone Help Clean up Supply Chains in the Smartphone Market?" *The Guardian* (19 September 2013). available at: https://www.theguardian.com/sustainable-business/fairphone-supply-chain-smartphone-market.
[232] Sam Phipps, "Case Study: How Fairphone Is Blazing a Trail to a Smarter Phone Industry" *Ethical Corporation*, (22 April 2016), available at: http://www.ethicalcorp.com/case-study-how-fairphone-blazing-trail-smarter-phone-industry.
[233] Fairphone, "Cost Breakdown of the First Fairphone" (September 2013), available at: https://www.fairphone.com/wp-content/uploads/2013/09/Fairphone_Cost_Breakdown_and_Key_Sept2013.pdf; Fairphone, "Cost Breakdown of the Fairphone 2" (2015), available at: https://www.fairphone.com/wp-content/uploads/2015/09/Fairphone2-Cost-Breakdown.pdf.
[234] Fairphone, "Fairphone 2 Supply Chain" *Sourcemap*, available at: https://open.sourcemap.com/maps/57d016b346a1127f1ceff50c.
[235] Fairphone, "Smartphone Material Profiles" (2017), available at: https://www.fairphone.com/wp-content/uploads/2017/05/SmartphoneMaterialProfiles_May2017.pdf.

SOMO, Südwind, and the Good Electronics Network pointed out that certain aspects had not been sufficiently addressed by the company.[236] In response, Fairphone published an article on its website aimed at addressing the issues mentioned in the report.[237]

Fairphone similarly has a novel approach to engagement with their own customers, insofar as the company has actively communicated about its emerging problems in its supply chain. For instance, when the production of their terminals was delayed in December 2015 due to a high volume of Christmas orders, the company issued a public statement explaining to their customers the reasons for the delay, which were to avoid supply chain workers working excessive hours.[238] In its communication, the company explained the implications of production requirements on the workforce.[239] The company has been hailed as meeting "their customer requirements by openly communicating sustainability achievements as well as shortcomings and how they deal with them".[240] Commentators have also noted that Fairphone's practices provide an example of how a transparent communication strategy can improve standards in a sector. If a company raises its standards, other business may "follow by raising their standards too due to competition reasons… in order to be able to sell their products on the market, or due to normative reasons".[241]

Despite this, Fairphone has not been exempt from criticism. Issues have been raised regarding the misuse of the word "fair", the impossibility of fair and sustainable production in trade union-free China – where the company's terminals are assembled – and the small size of Fairphone's actual impact.[242]

Yet, the company has been put forward by Oxfam as an example of a more "equitably structured business" which is "governed to prioritise a social mission",[243] and an innovative electronics company "building their brand appeal on the basis of fair work conditions".[244] The above report by SOMO et al states that Fairphone standards scored higher than those of the sustainability certification awarded to IT products by the Swedish company TCO Development.[245]

Fairphone provides an interesting example through the way in which the company has communicated its actions in an unprecedented way, and how a small company can aim to raise standards and awareness amongst their very large competitors.

4.9 Communication with stakeholders and local experts

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[236] The "aspects not sufficiently addressed by Fairphone" were: (i) the improvement of recyclability through the design; (ii) the promotion of responsible use of chemicals during production; (iii) no mention of an environmental management system; (iv) no effective grievance mechanisms at the factory level; and (v) no mention of responsible taxation. See SOMO, Südwind and GoodElectronics Network, "TCO Certified Smartphones versus Fairphone. A Comparison of Sustainability Criteria" (2015), available at: https://www.somo.nl/wp-content/uploads/2015/07/TCO-Certified-Smartphones-versus-Fairphone.pdf at 38.
[237] Fairphone, "Comparing Fairphone's Approach to a Sustainability Label" (23 July 2015), available at: https://www.fairphone.com/en/2015/07/23/comparing-fairphones-approach-to-a-sustainability-label/.
[238] Fairphone, "December Production Update: How Production, Workforce and Delivery Are Intertwined" (3 December 2015), available at: https://www.fairphone.com/en/2015/12/03/december-production-update-how-production-workforce-and-delivery-are-intertwined/.
[239] Ibid.
[240] Carolin Brix-Asala et al "Sustainability Tensions in Supply Chains: A Case Study of Paradoxes and Their Management" (2018) 10 *Sustainability* 424 at 13.
[241] Sarah Van Eynde and Kris Bachus, "Non-State Participation in Sustainable Materials Management: The Case of Fairphone" *Policy Research Centre on Sustainable Materials Management* (2016), available at: https://lirias.kuleuven.be/1864104 at 4.
[242] SOMO, Südwind and GoodElectronics Network above n 236 at 30.
[243] Oxfam et al, "Reward Work, Not Wealth: To End the Inequality Crisis, We Must Build an Economy for Ordinary Working People, Not the Rich and Powerful" (2018), available at: https://www-cdn.oxfam.org/s3fs-public/file_attachments/bp-reward-work-not-wealth-220118-en.pdf at 53.
[244] Earth Security Group, "The Earth Security Report 2017: Sustainable Development Goals for Business Diplomacy and Growth" (2017), available at: http://www.indiaenvironmentportal.org.in/files/file/The-Earth-Security-Report-2017.pdf at 48.
[245] SOMO, Südwind and GoodElectronics Network above n 236. See also TCO Development website at: https://tcocertified.com/.

As discussed in the Regulatory Review, the concept of due diligence as derived from the UNGPs into other standards such as the OECD Guidelines requires the company to "go beyond" the risks to the company to focus on the risks *to those affected* (the "rights-holders").[246] A survey respondent from a large cross-sectoral industry organisation emphasized in an optional text box that this requires a change in the traditional way in which companies have approached due diligence:

> Several [of our] members have strived to identify best practices and key factors for success in deploying due diligence processes in their own operations and through supply chains. Among these key factors are … Changing the point of view: the targeted risks are not those for the company, but risks to society and to the environment.

They added that:

> Reporting adopted diligence measures is more than "top down communication" and disclosing regulated information. It is also about engaging with stakeholders and responding to their concerns … Adjusting the content and form of communication so that it is accessible, understandable and relevant for its recipients … Providing information which allows stakeholders to assess the way the company considers the impacts of its activities, the way it selects the information that is disclosed and the challenges and lessons learnt etc.

In one example of a partnership with stakeholders and local experts, an interviewee from a multinational garment company indicated:

> We have a global framework agreement with IndustriAll global union, with the trade unions. And we do work with the trade unions on a daily, daily, and I really mean it, daily basis, on the ground. We'll go to factories with them. We will travel with them to specific factories because something is going on, or we will travel to a specific region to put together their understanding of what workers need, to understand which type of project could improve not only factory by factory but also the region. Our work with trade unions for the last 11 years has been and still is very interesting for everyone. It's also challenging because we work with IndustriAll on a global level, but then we also work with local trade unions, and each country has its own local reality, even the maturity of the trade unions is completely different.

Case study: Nestlé and NGO partnering

Nestlé, domiciled in Switzerland, is one of the largest food and beverage companies in the world, with an extensive supply chain. This case study provides an illustrative example on how partnering with a human rights organisation may assist a company to prevent and address human rights impacts along their supply chain.

Since 2010, Nestlé has been collaborating with the Danish Institute for Human Rights ("DIHR") under an innovative partnership aimed at integrating human rights into Nestlé's policies and procedures.[247] As a product of this alliance, Nestlé has developed and implemented a Human Rights Due Diligence Programme based on eight pillars, in which human rights impact assessments ("HRIAs") have been central. Under this partnership, the DIHR has conducted research on parts of Nestlé's supply chain. For example, in 2013 both the DIHR and Nestlé published a report presenting the

[246] Commentary to UNGP 17.
[247] Danish Institute for Human Rights ("DIHR") "Nestlé Partnership", available at: https://www.humanrights.dk/projects/nestle-partnership.

methodology and findings of seven human rights impact assessments conducted in country operations of Nestlé.[248] In April 2014, this report was followed by a roundtable facilitated by the DIHR, with around twenty experts on human rights and development from consultancy firms, think thanks, international organisations and NGOs.[249] This multi-stakeholder engagement is a novel approach to managing due diligence in the supply chain.

In a report in 2016 Nestlé's practices in its supply chain were considered as "notable examples" on traceability, cascading standards through the supply chain, and workers voice.[250]

More recently, in 2018, the DIHR and The Forest Trust published an assessment of labour's rights in Nestlé's palm oil supply chain in Indonesia.[251] This report assessed the company's direct and indirect suppliers to identify and describe actual and potential human rights risks and impacts, with a particular focus on labour rights. As a result, both Nestlé and Golden Agri-Resources – Nestlé's main oil palm supplier in Indonesia – developed and published plans to address the conclusions of the assessment.[252]

In December 2018 Nestlé announced an improved version of its human rights training to commemorate the 70th Anniversary of the Universal Declaration of Human Rights,[253] and in April 2019, the company made its human rights training publicly accessible, becoming the first company to do so.[254]

Nevertheless, this engagement towards a human rights-compliant supply chain does not seem to have prevented lawsuits from being filed against Nestlé.[255] This raises questions on the counter-effects of a company's public engagement in due diligence in its supply chain. It has been suggested that companies may fear that the more they publish, the more they will be exposing themselves to be possible legal claims, thereby creating a legal incentive not to publish nor engage in due diligence.[256] As Nestlé representatives have stated in response to claims filed against the company, "in bringing such lawsuits,

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[248] DIHR and Nestlé, "Talking the Human Rights Walk" Nestlé's Experience Assessing Human Rights Impacts in Its Business Activities" (2013), available at: http://www.nestle.com/asset-library/documents/library/documents/corporate_social_responsibility/nestle-hria-white-paper.pdf.
[249] SustainAbility, "Nestlé Human Rights and Rural Development Roundtable London: Summary of Stakeholder Feedback" (2014), available at: https://www.humanrights.dk/sites/humanrights.dk/files/media/dokumenter/business/nestle-human-rights-rural-development-stakeholder-summary.pdf.
[250] Know the Chain, "Food & Beverage Benchmark Findings Report: How Are 20 of the Largest Companies Addressing Forced Labor in Their Supply Chains?" (2016), available at: https://ktcdevlab2.wpengine.com/wp-content/plugins/ktc-benchmark/app/public/images/benchmark_reports/KTC_Food_Beverage_Findings_Report_October.pdf at 12, 14 and 16.
[251] Dirk Hoffmann, Tulika Bansal and Janhavi Naidu, "Labour Rights Assessment: Nestlé's Palm Oil Supply Chain in Indonesia" DIHR and The Forest Trust (2018), available at: https://www.humanrights.dk/sites/humanrights.dk/files/media/dokumenter/udgivelser/hrb_2018/nestle-rapport_hria_2018.pdf.
[252] Nestlé, "Nestlé Action Plan on Labour Rights in Palm Oil Supply Chains" (2018), available at: https://www.nestle.com/asset-library/documents/creating-shared-value/responsible-sourcing/palm-oil-action-plan-2018.pdf; Golden Agri-Resources, "GAR Supplier Support Action Plan: GSEP Principle 3 – Work Environment and Industrial Relations" (2018), available at: https://goldenagri.com.sg/wp-content/uploads/2017/06/Action-Plan-HRIA-V8clean.pdf.
[253] Yann Wyss, "Building Human Rights Capabilities Where It Matters", Nestlé, available at: https://www.nestle.com/stories/building-human-rights-capabilities.
[254] DIHR, "Nestlé First Company to Publicly Share Its Human Rights Training for Employees", available at: https://www.humanrights.dk/news/nestle-first-company-publicly-share-its-human-rights-training-employees.
[255] For instance, see BHRRC "Nestlé, Cargill, Archer Daniels Midland Lawsuit (Re Côte d'Ivoire)", available at: https://www.business-humanrights.org/en/nestl%C3%A9-cargill-archer-daniels-midland-lawsuit-re-c%C3%B4te-divoire. BHRRC, "Nestlé Lawsuit (Re Forced Labour in Thai Fishing Industry)", available at: https://www.business-humanrights.org/en/nestl%C3%A9-lawsuit-re-forced-labour-in-thai-fishing-industry; Nick Brown, "Court Dismisses Cocoa Supply Chain Labor Non-Disclosure Suit Against Nestlé", *Daily Coffee News by Roast Magazine* (12 March 2019), available at: https://dailycoffeenews.com/2019/03/12/court-dismisses-cocoa-supply-chain-labor-non-disclosure-suit-against-nestle/; and Emily Field, "'Sustainable" Nestle Cocoa Made With Child Slavery, Suit Says", Law 360 (24 April 2019), available at: https://www.business-humanrights.org/en/usa-class-action-lawsuit-filed-against-nestle-for-child-slavery-on-cocoa-harvest-in-west-african-farms.
[256] For example, see Peter Nestor and Jonathan Drimmer "How Companies Should Respond to the Vedanta Ruling", *BSR*, 30 April 2019, available at: https://www.bsr.org/en/our-insights/blog-view/how-companies-should-respond-to-the-vedanta-ruling.

the plaintiffs' class action lawyers are targeting the very organisations trying to fight forced labor".[257]

In any event, Nestlé represents an excellent example of how meaningful and ongoing stakeholder dialogue, engagement with human rights experts and local partners, and reporting can contribute to effective due diligence in supply chains.

Case study: Huayou Cobalt: Acknowledging risks in artisanal and small-scale mining

Huayou Cobalt is a Chinese company. It is one of the world's largest manufacturers of cobalt products. In the Democratic Republic of the Congo ("DRC"), it operates with its wholly owned subsidiary Congo Dongfang International Mining SARL ("CDM"). For the purposes of this case study, Huayou and CDM will be considered as one company.

In a report published in 2016, Amnesty International traced cobalt from artisanal mines throughout the supply chain. It found that CDM was one of the largest companies in the DRC buying cobalt ores from licensed trading houses, which were in turn purchasing cobalt mineral from artisan miners.[258]

The DRC holds nearly half of the world's cobalt resources and concentrates more than half of the world's mined production.[259] Cobalt is an essential mineral for the production of electrical batteries, which in turn is increasingly being relied on in the shift to more sustainable energy. As such, this case study is particularly relevant to this study in light of the EU's commitments to achieving net-zero greenhouse gas emissions.[260]

Most of the cobalt extraction of it in the DRC is made by artisanal and small scale mining, a sector with high risks of child labour and other human rights abuses. In particular, Amnesty International highlighted in its report that most of the miners worked for very long hours in unsupported hand-dug tunnels without the most basic of protective equipment.[261] As a consequence, the workers faced high risk of long-term health damage and fatal accidents. Young children worked for up to twelve hours a day "scaven[ging] for rocks containing cobalt in the discarded by-products of industrial mines, before washing and sorting the ore to sell".[262]

Following the publication of the report, Huayou acknowledged in a letter to Amnesty International that it previously had a deficit in the awareness of human rights risks and abuses along its supply chain.[263] Since then, the company started taking steps to improve the international human rights standards in its supply chain.[264] Huayou sent representatives to consult with experts at the OECD, undertook a fact-finding exercise in the DRC, met with DRC government mining authorities and visited the same artisanal mining sites that Amnesty International reported.[265] In particular, Huayou did not

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[257] Field above n 255.
[258] Amnesty International, "'This Is What We Die for': Human Rights Abuses in the Democratic Republic of the Congo Power the Global Trade in Cobalt" (2016), available at: https://www.amnesty.org/download/Documents/AFR6231832016ENGLISH.PDF at 47.
[259] Fairphone, "Smartphone Material Profiles" above n 235 at 8.
[260] For example, see Communication from the Commission to the European Parliament, the European Council, the Council, the European Economic and Social Committee, the Committee of the Regions and the European Investment Bank "A Clean Planet for all: A European strategic long-term vision for a prosperous, modern, competitive and climate neutral economy", COM(2018) 773, 28 November 2018, available at: https://ec.europa.eu/clima/sites/clima/files/docs/pages/com_2018_733_en.pdf.
[261] Amnesty International above n 258.
[262] Ibid at 4.
[263] Amnesty International, "Time to Recharge: Corporate Action and Inaction to Tackle Abuses in the Cobalt Supply Chain" (2017), available at: https://www.amnesty.org/download/Documents/AFR6273952017ENGLISH.PDF at 38.
[264] Bryce Lee, "Sustainable Supply of Li-Ion New Battery Materials" *Cobalt Institute (CI) Conference 2018*, Las Vegas (24 May 2018), available at: http://www.huayou.com/downloadRepository/5af6fe72-d1ab-4296-9dd0-07d275640250.pdf at 10.
[265] Amnesty International above n 263 at 38.

terminate its relationships with its suppliers sourcing from artisanal and small scale mines.[266] In acknowledging that abandoning the artisanal and small scale miners would create a negative impact in the communities which subsist from these practices, the company put in place due diligence policies along its supply chain.

Since 2017, Huayou requires its suppliers to sign three documents which are in line with the OECD guidance: a Due Diligence Policy for a Responsible Global Supply Chain of Cobalt,[267] a Suppliers' Code of Conduct,[268] and a Supplier Standard for Responsible Sourcing of Cobalt.[269] According to its new due diligence scheme, Huayou will stop buying cobalt from suppliers which do not know the source of the cobalt sourced from artisanal small scale miners, do not have strong controls of risks in place, or do not have a proper tracking system.[270] Moreover, Huayou put in place a strategy to map and mitigate risks in its supply chains by differentiating between "Type 1 mines", being former industrial mines turned into artisanal cooperatives, and "Type 2 mines", which are mines located within residential areas.

In 2017, Amnesty International published a follow-up report in which it assessed the supply chain due diligence schemes put in place by Huayou in the DRC.[271] Amnesty International acknowledged that: "Since January 2016, Huayou Cobalt has taken steps to establish a cobalt supply chain due diligence policy and management system in line with international standards [e.g. OECD Guidance and CCCMC Guidelines] to investigate and map its supply chain and to start to mitigate risks associated with artisanal mining".[272]

Nevertheless, Amnesty International also noted that: "much more concrete detail is needed about potential and actual risks the company has identified in the DRC, as well as results of Huayou Cobalt's risk assessment activity… Without this information, it is difficult to assess the quality and effectiveness of Huayou Cobalt's risk assessment and mitigation work."[273]

In response to the report, Huayou stated that: "In the absence of legal or generally acknowledged due diligence guidelines and clear requirements regarding due diligence information reporting, and when other companies are not subject to the same scrutiny as Huayou, we believe that it will create an unfair business environment if Huayou unilaterally makes detailed due diligence investigation public. Even so, Huayou is currently the most transparent business in the industry."[274] Further, Huayou also declared that "its efforts to exercise leverage over its suppliers have been weakened by the presence of other large buyers who do not face the same pressure to undertake supply chain due diligence because they have not been publicly identified as having supply chain risks".[275]

Huayou's case study shows a very strong engagement with Amnesty International in an attempt to set up and improve due diligence practices along its upstream supply chain. This case study suggests that supply chain due diligence can be carried out, even in sectors where human rights risks are very high. It also shows that companies which

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266 Ibid.
267 Huayou Cobalt, "Due Diligence Policy for a Responsible Global Supply Chain of Cobalt", available at: http://en.huayou.com/downloadRepository/8adb91b3-b766-453c-97eb-e9f388b7d814.pdf.
268 Huayou Cobalt, "Suppliers' Code of Conduct", available at: http://en.huayou.com/downloadRepository/e6cefb0e-c623-4a9a-a29e-3ed3e6a89c96.pdf.
269 Huayou Cobalt, "Supplier Standard for Responsible Sourcing of Cobalt", available at: http://en.huayou.com/downloadRepository/49407ec9-ca3a-43ee-8b88-2cec3bea0850.pdf.
270 Bryce Lee, "Huayou Cobalt's Due Diligence and Audit of Responsible Cobalt Supply Chain" (9 August 2017), available at: http://en.huayou.com/downloadRepository/ce6d255e-2a81-4718-bd51-7f6f85f0ed5d.pdf at 25.
271 Amnesty International above n 263.
272 Ibid at 44–45.
273 Ibid at 45.
274 Ibid.
275 Ibid at 40.

have been identified by civil society as adversely affecting human rights in their supply chains, can take proactive steps to improve to the point that they might be seen as the leaders in their sector by those same civil society organisations.

This case study also provides a concrete example of a company which has publicly explained that its due diligence efforts are less effective if other large buyers, which source from the same suppliers, are not adhering to the same standard.

4.10 Buying practices and an integrated approach

Many stakeholders in the interviews and surveys highlighted that buying practices, including price, are a major contributor to adverse impacts in the supply chain, and accordingly need to be considered as part of a due diligence standard.

The Joint Ethical Trading Initiatives (ETI) have issued a guide on how to buy responsibly which aims to develop and implement responsible purchasing practices. The guide presents and builds on findings of a survey of almost 1,500 suppliers to UK, Denmark and Norway-based companies across multiple sectors.[276] The survey found that "[w]hile many companies require suppliers to respect their codes of conduct (CoC) and monitor suppliers' labour rights performance, their buying practices often sit at odds with these initiatives."[277] While 93% of surveyed suppliers indicated that they are required to follow codes of conduct, "many customers do not provide sufficient support to help [suppliers] meet these requirements of their code of conduct", with 48% of suppliers receiving "no help at all".[278]

An interviewee from an international civil society organisation explained this issue as follows:

> [W]e've noticed…sometimes companies, if they do human rights due diligence, then they would just say to their suppliers: 'Oh, you have to sign this code of conduct. You cannot use children, you cannot do this, you cannot do that.' But they still have the same trading conditions. The same price, the same delivery time and so on. So it really pushes the pressure on the supplier without the buyer having to do anything about it ... Especially if it's small producers, small cooperatives, or small companies. They really struggle. They have increased pressure. They need to produce in a sustainable way, which is a good thing, but if they don't get paid enough, it's very difficult for them…

One interviewee from a multinational corporation which organizes workshops on their due diligence practices and carry out a number of interviews, including with their suppliers, indicated:

> [I]t was so interesting to talk to suppliers who shared their dilemmas. You know, they are put under pressure by us on quality, service level, on price, on timing, on speed, and at the same time we expect them to make sure that their own suppliers are supervised. And they say: 'Great, where is the support from [your company]?' Then you really get to understand the local context, which is very powerful. And then that information you bring into the workshop [...] It's so

[276] The Joint Ethical Trading Initiatives ("ETI"), "Guide to buying responsibly" (2018), available at: https://www.ethicaltrade.org/resources/guide-to-buying-responsibly, for which the authors interviewed over 1500 suppliers about buying practices including price.
[277] Ibid at 7.
[278] Ibid.

powerful because it opens people's eyes. The personal engagement and taking the time is quite powerful.

Another interviewee who works with businesses in the implementation of the UNGPs highlighted how purchasing practices can contradict a company's supply chain standards due to a lack of internal integration between the functions of the company:

> Where we often see the process getting a bit stuck is at the step immediately after assessment which is integration, taking action as we call it in the [UN]GPs or the 'so what?'. You go through your identification exercise, you also go through prioritisation, as that's something that the [UN]GPs allow for, and is necessary often for companies with huge numbers of risks and impacts to make their choices. But then really moving into parts of business practice that are going to be most meaningful in terms of really responding to those risks. I'm talking here here things like purchasing practices … It's not about having one-off ad hoc initiatives, it's not about increasing your audit programs. It's about tackling the parts of the business where decisions are being made or have been made for a long time on a different set of criteria, and where you have potentially conflicting incentives internally. So you have your human rights, or they may be framed more broadly as sustainability commitments, and then, on the other hand, you have purchasing teams who have been given very clear instructions that they have to prioritize price, and quality and timeliness. And until these things are really brought together by the business, you're almost asking staff to do something impossible. You're asking them to sort of put one set of values over business priorities, and it's not fair to put that on operational staff. These are decisions that are integral to the business model really, and to whether a business accepts that there may be some real costs of taking meaningful measures of the kind that the UNGPs and human rights due diligence are asking for.

The interviewee went on to add that there is a risk if regulation focuses too much on "public-facing" parts, such as reporting and transparency:

> [If] legislation focuses too much on the public-facing parts of due diligence, if it's legislation that doesn't really give guidance about 'this means risks to people, and it means getting into difficult parts of the business like purchasing practices', if it doesn't incentivize the right kinds of behaviour change by business.

One interviewee who works with companies on their due diligence practices also referred to other initiatives such as:

> Better Buying and a number of other self-assessment tools where big brands allow suppliers to rate their purchasing practices, which feeds into their due diligence work. It supplies and provides brands with an honest assessment of whether their payment terms are for example, are undermining labour rights…[It] is really promising because it allows suppliers to provide anonymous feedback so brands don't know who submitted the feedback form. Brands only receive the reply when suppliers provide feedback, and it holds a bit of a mirror upward in terms of knowing what practices suppliers value and what [they don't like].

With regard to integrated buying practices, one interviewee from a multinational company indicated:

> We create teams within our teams so that they could focus on creating global solutions for these rights, instead of always going factory by factory case by case and always having a reactive approach to the impacts.

One interviewee from a civil society organisation explained how buying practices, including price, could by tied with the legal standard of care of mandatory due diligence, including a due diligence defence:

> We are really supportive of [a mandatory due diligence law], but we want to make sure that it is done in a way that does not just put the pressure on the suppliers, but ensures that everyone along the chain takes their responsibility. And for us, really, the responsibility of the buying company is the way they buy. It's not to go and build a school in Africa so that there is no child labour. It's not to go and send auditors every year or every month to check that there are no children working on the farms. It's really the way they buy and how much they pay.
>
> If a company pays a good price, then it's up to the supplier to respect human rights. Now, if they still violate human rights, or if they still, I don't know, don't pay minimum wages even though the price they get is sufficient, then it's not really the fault of the company. But if companies pay a really low price, then, I mean, they can't say: 'Oh, we didn't know'. They didn't give the means for the supplier to actually respect human rights. Now I know it is easier said than done, because it's really difficult, and you touch on the price, and we can't define the price in a law. How are they going to calculate the costs of production? That is actually why the Fairtrade model is quite interesting, because, it's not perfect, but [it calculates] a minimum price which would cover, on average, the costs of sustainable production.

Case study: Buying practices and the Fairtrade Minimum Price for cocoa

Fairtrade is a non-for-profit organisation campaigning for companies to pay sustainable prices and provide for decent working conditions and local sustainable production.[279] It is now a global movement with its most active presence in the United Kingdom under the Fairtrade Foundation. Fairtrade also runs a certification scheme known as FAIRTRADE Mark, which means that farmers will benefit from "the protection of the Fairtrade Minimum Price (where relevant) and the Premium to choose how to invest in their community".[280]

The Premium "is an amount on top of the selling price, paid directly to farmer organisations to spend on projects of their choice".[281] It is calculated as a percentage of the amount of produce sold, and helps farmers and workers to ameliorate their cooperatives and improve their conditions.[282]

The Minimum Price "defines the lowest possible price that a buyer of Fairtrade products must pay the producer'.[283] It is set following a "consultative process with Fairtrade farmers, workers and traders and guarantees that producer groups receive a price which covers what it costs them to grow their crop".[284] Fairtrade has also drafted Guidelines for Evaluating the Costs of Sustainable Production ("COSP"), which are a central source

[279] Fairtrade, "Who We Are", available at: http://www.fairtrade.org.uk/What-is-Fairtrade/Who-we-are.
[280] Fairtrade, "Using the Fairtrade Mark", available at: https://www.fairtrade.org.uk/What-is-Fairtrade/Using-the-FAIRTRADE-Mark.
[281] Fairtrade, "Cocoa Farmers to Earn More through a Higher Fairtrade Minimum Price", (3 December 2018), available at: https://www.fairtrade.org.uk/Media-Centre/News/December-2018/Cocoa-farmers-to-earn-more-through-a-higher-Fairtrade-Minimum-Price.
[282] Fairtrade, "Fairtrade Premium", available at: https://www.fairtrade.org.uk/What-is-Fairtrade/What-Fairtrade-does/Fairtrade-Premium.
[283] Fairtrade, "Frequently Asked Questions", available at: http://www.fairtrade.org.uk/What-is-Fairtrade/FAQs.
[284] Ibid.

of data for the development of the Minimum Prices, which intend to cover, on average, the COSP of all producers within the system.[285] In any case, if market prices are higher than the Minimum, Fairtrade traders must pay the market price.

With over the 60% of global cocoa production taking place in Côte d'Ivoire and Ghana, and 90% of world's cocoa production grown on small family farms,[286] cocoa farmers are one of the sectors included within Fairtrade's schemes. In December 2018, Fairtrade announced an increase of 20% in the Minimum Price and the Premium of cocoa from October 2019. Accordingly, the Minimum Price for conventional cocoa will be raised "from $2,000 to $2,400 per metric tonne at the point of export (FOB)", and the Premium will be of $240 per metric tonne.[287]

This increase was introduced in response to the challenges that the West African cocoa sector faces. In a study published in April 2018, Fairtrade showed that "58% of Fairtrade certified cocoa farming households in Côte d'Ivoire had incomes below the extreme poverty line".[288] Hence, the new Minimum Price will enable average Fairtrade cocoa farmers to earn above the extreme poverty line.

Nevertheless, the new Minimum Prices do not equal a living income for cocoa farmers. Fairtrade has determined a Living Income Reference Price for cocoa in Côte d'Ivoire and Ghana, but, unlike the Minimum Price, it is not mandatory for the Fairtrade mark.[289]

The Fairtrade pricing schemes do not require due diligence. However, it is possible that any due diligence standard of care would need to take into account the industry standards set by established mechanisms such as Fairtrade, particularly in sectors such as cocoa where prices have been developed to reflect living wage.

4.11 Remedies and grievance mechanisms

One component of due diligence is the creation of operational-level grievance mechanisms for the identification, and where relevant remediation, of impacts. However, stakeholders highlighted that current grievance mechanisms often fall short in various respects.

An interviewee who works with businesses in the implementation of the UNGPs explained that:

> Grievance mechanisms can perform a due diligence role as well as a remediation role. You certainly see stronger grievance mechanisms in connection with the companies' own operations, as that's where everybody knows that they need to have hotlines or speak up mechanisms or open doors policies, or things that feel like more traditional territory. How you translate that thinking into a supply chain context, they still struggle with.

One interviewee from an international trade association, which works with companies on their due diligence practices, indicated:

[285] Fairtrade International, "Guidance for Estimating Costs of Sustainable Production" (2011), available at: https://www.fairtrade.net/fileadmin/user_upload/content/2009/standards/documents/3.1_Guidance_COSP_EN_2011-11-21.pdf.
[286] Fairtrade, "Cocoa Farmers", available at: https://www.fairtrade.org.uk/Farmers-and-Workers/Cocoa.
[287] Fairtrade "Cocoa Farmers to Earn More…" above n 281. The price for organic cocoa will be $300 higher than the market price or the Minimum Price, whichever is higher. Further, the Premium will be now the highest of any Fairtrade certification.
[288] Fairtrade International, "Cocoa Farmer Income: The Household Income of Cocoa Farmers in Côte d'Ivoire and Strategies for Improvement" (April 2018), available at: https://www.fairtrade.net/fileadmin/user_upload/content/2009/resources/2018-04_Management_Response_CDI_Cocoa_Household_Income_Study.pdf.
[289] Fairtrade "Cocoa Farmers to Earn More…" above n 281.

It seems like, for example, grievance mechanism, the intermediary will know that at that big farm, there might be 10 posters in the room with 10 different hotlines but through the supermarkets, they've developed their own grievance process. They've demanded that every supplier post their phone number on the poster on the factory or farm rules as part of their terms and conditions and their code of conduct.

They're doing so probably because they think it might be the right thing to do, but the consequences that the big intermediary will have a ridiculous number of colourful posters with a dozen different phone numbers for workers to contact, no worker knows which of the phone numbers they should be contacting if there's a problem and they don't trust any of the hotlines because they're all linked to the company. It's an international company. They don't know who they're speaking to and what the process is.

Case study: The Bangladesh Accord and Worker Safety

On 24 April 2013 the Rana Plaza building in Dhaka, Bangladesh, collapsed, killing more than 1,100 and injuring over 2,500 persons.[290] It was at the time the deadliest disaster in the history of garment industry and made the poor labour conditions faced by workers in the ready-made garment (RMG) sector in Bangladesh which gained attention in the Western world.[291]

Following the collapse, brands and retailers joined efforts to address "long-standing governance gaps around health and safety issues in garment production sites".[292] This resulted in two competing initiatives: the Accord on Fire and Building Safety in Bangladesh,[293] and the Alliance for Bangladesh Worker Safety.[294] The Accord in particular provides an example of how multi-stakeholder collective agreements, ultimately led by companies, can lead to binding due diligence obligations and effective remedies for victims, even where local law enforcement structures have failed.[295] The Accord was signed in May 2013 and consists of a five-year legally binding agreement between over two hundred mostly European garment brands and retailers and two global unions (IndustriALL and UNI Global Union), as well as several local trade unions and witness signatories.[296]

The Accord provided for an independent inspection programme, public disclosure of all factories, inspection reports and corrective action plans, a commitment by signatory brands to ensure sufficient funds are available for remediation, democratically elected health and safety committees in all factories, and worker empowerment.[297] Prior to the

[290] International Labour Organization ("ILO") "The Rana Plaza Accident and Its Aftermath", (21 December 2017), available at: http://www.ilo.org/global/topics/geip/WCMS_614394/lang--en/index.htm.
[291] Julfikar Ali Manik and Jim Yardley, "Scores Dead in Bangladesh Building Collapse" *The New York Times* (19 October 2018); Jim Yardley, "Bangladeshi Lab Struggles to Identify Rana Plaza's Dead" *The New York Times* (19 October 2018); The Editorial Board, "One Year After Rana Plaza" *The New York Times* (20 December 2017).
[292] Dorothée Baumann-Pauly, Sarah Labowitz and Nate Stein, "Transforming the Garment Industry in Bangladesh: Sharing Responsibility" in Sarah Margaretha Jastram and Anna-Maria Schneider (eds), *Sustainable Fashion : Governance and New Management Approaches*, Springer International Publishing (2018) 41.
[293] The Accord on Fire and Building Safety in Bangladesh, available at: https://www.business-humanrights.org/en/the-accord-on-fire-and-building-safety-in-bangladesh.
[294] Alliance for Bangladesh Worker Safety, available at: http://www.bangladeshworkersafety.org/.
[295] Jimmy Donaghey and Juliane Reinecke, "When Industrial Democracy Meets Corporate Social Responsibility — A Comparison of the Bangladesh Accord and Alliance as Responses to the Rana Plaza Disaster" (2018) 56 *British Journal of Industrial Relations* 14 at 2.
[296] Bangladesh Accord on Fire and Building Safety, "Accord Signatories", available at: https://bangladeshaccord.org/signatories.
[297] Accord above n 293.

expiration of the Accord's five-year term, it was succeeded by the "2018 Accord on Fire and Building Safety in Bangladesh", which entered into force on 31 May 2018,[298] but was not signed by all the companies that entered into the Accord in 2013.[299]

One of the most innovative aspects of the Accord was its enforceable nature through arbitration and 'inclusivity of supplier employees via their representatives'.[300] However, the binding nature of these aspects deterred a number of US companies from participating in the Accord.[301]

Instead, in July 2013 a number of US garment companies, which had not signed the Accord, launched the Alliance for Bangladesh Worker Safety.[302] This initiative was 'built upon a fairly traditional CSR-based approach, resulting in collective, transnational industry self-regulation'.[303] The Alliance did not require participating companies to contribute any funds, lacked enforcement provisions, was negotiated without worker representatives and did not provide for a space for worker representatives in its governance.[304] These shortcomings made critics consider the Alliance 'as an effort to undercut the Accord by providing a less onerous and less rigorous alternative'.[305]

The Alliance ceased its activity on 31 December 2018, and was not continued by a subsequent agreement.[306] The members of the initiative argued that "with an ecosystem of safety now in place", they were transitioning to "work through a locally-based organisation to collectively monitor safety standards".[307] Critics have noted that "it is by far too early to state [that]… at present the RMG is safe with regard to fire safety".[308]

Both the Accord and the Alliance have been deemed positive interventions in Bangladeshi RMG sector, as they have shown that collective inspections can improve workers' safety.[309] Most particularly, the Accord represents a novel example, insofar as it is binding, inclusive and enforceable.[310] It is also noticeable that the Accord's the enforcement mechanism appears to work. Two arbitrations cases raised by unions against fashion brands which were in breach of the agreement were settled before the Permanent Court of Arbitration in 2018.[311]

These examples, and in particular the Accord, present examples of how companies can collectively provide for binding obligations to improve human rights conditions in the supply chain, even in a notoriously high risk sector and country. In the case of the Accord these obligations included commitments to provide financial resources towards improvements in suppliers' factories, and enforceable arbitration mechanisms which

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[298] 2018 Accord on Fire and Building Safety in Bangladesh, available at: https://admin.bangladeshaccord.org/wp-content/uploads/2018/08/2018-Accord.pdf.
[299] Industriall, "Brands that have not signed the 2018 Accord" (30 August 2018), available at: http://www.industriall-union.org/brands-that-have-not-signed-the-2018-accord.
[300] Jaakko Salminen, "The Accord on Fire and Building Safety in Bangladesh: A New Paradigm for Limiting Buyers' Liability in Global Supply Chains?" (2018) 66 *The American Journal of Comparative Law* 411 at 416.
[301] Ibid.
[302] Alliance for Bangladesh Worker Safety above n 294.
[303] Donaghey and Reinecke above n 295 at 2.
[304] Mark Anner, Jennifer Bair and Jeremy Blasi, "Toward Joint Liability in Global Supply Chains: Addressing the Root Causes of Labor Violations in International Subcontracting Networks" (2013) 35 *Comparative Labor Law & Policy Journal* 1 at 30.
[305] Ibid.
[306] Alliance for Bangladesh Worker Safety above n 294.
[307] Alliance for Bangladesh Worker Safety, "Alliance Fifth Annual Report 2018", (11 December 2018), available at: http://www.bangladeshworkersafety.org/488-2018-annual-report-press-release.
[308] Erik Wiersma, "Fire Safety in the Ready-Made Garment Industry in Bangladesh, Five Years after Rana Plaza", *Safety in The Garment Industry, Five Years After Rana Plaza* (2018), available at: https://www.researchgate.net/profile/Erik_Wiersma2/publication/326175338_Fire_Safety_in_the_Ready-Made_Garment_Industry_in_Bangladesh_Five_Years_after_Rana_Plaza/links/5b3c702ca6fdcc8506eeeee3/Fire-Safety-in-the-Ready-Made-Garment-Industry-in-Bangladesh-Five-Years-after-Rana-Plaza.pdf at 23.
[309] Donaghey and Reinecke above n 295 at 25.
[310] Salminen above n 300 at 450.
[311] Permanent Court of Arbitration, "Bangladesh Accord Arbitrations", available at: https://pca-cpa.org/en/cases/152/; Covington "Covington Helps Secure Historic Settlement in Arbitration under the Accord on Fire Building Safety in Bangladesh", (22 January 2018), available at: https://www.cov.com/en/news-and-insights/news/2018/01/covington-helps-secure-historic-settlement-in-arbitration-under-the-accord-on-fire-and-building-safety-in-bangladesh.

have led to real-life compensation and remedy for victims.

4.12 Incentives for undertaking due diligence

Survey respondents were asked for their views on what is, or will become, companies' main incentives to undertake due diligence for these impacts through the supply chain.

When asked about what the primary incentives for undertaking due diligence is, or have been, it is noticeable that the top three incentives selected by business respondents (in the business survey) and industry organisations (in the general stakeholder survey) were the same and in the same order: The top incentive for undertaking due diligence was reputational risks (66.19% for business respondents, 65.52% for industry organisations), followed by investors requiring a high standard (51.08% for business respondents, 55.17% for industry organisations), and consumers requiring a high standard (46.76% for business respondents, 55.17% for industry organisations).

This demonstrates that despite a divergence in views on regulatory options between these two groups (discussed below), industry organisations have a real understanding of the risks and incentives which drive business to undertake due diligence.

For business respondents, these incentives were followed by operational risks (42.25%), which, after financial risk (51.72%) was also the fifth top selected incentive selected by industry organisations (44.83%). Regulation requiring reporting on steps taken was the fifth most selected incentive by business respondents (41.73%). This was followed by financial risks (41.01%) and employees requiring a high standard (36.69%).

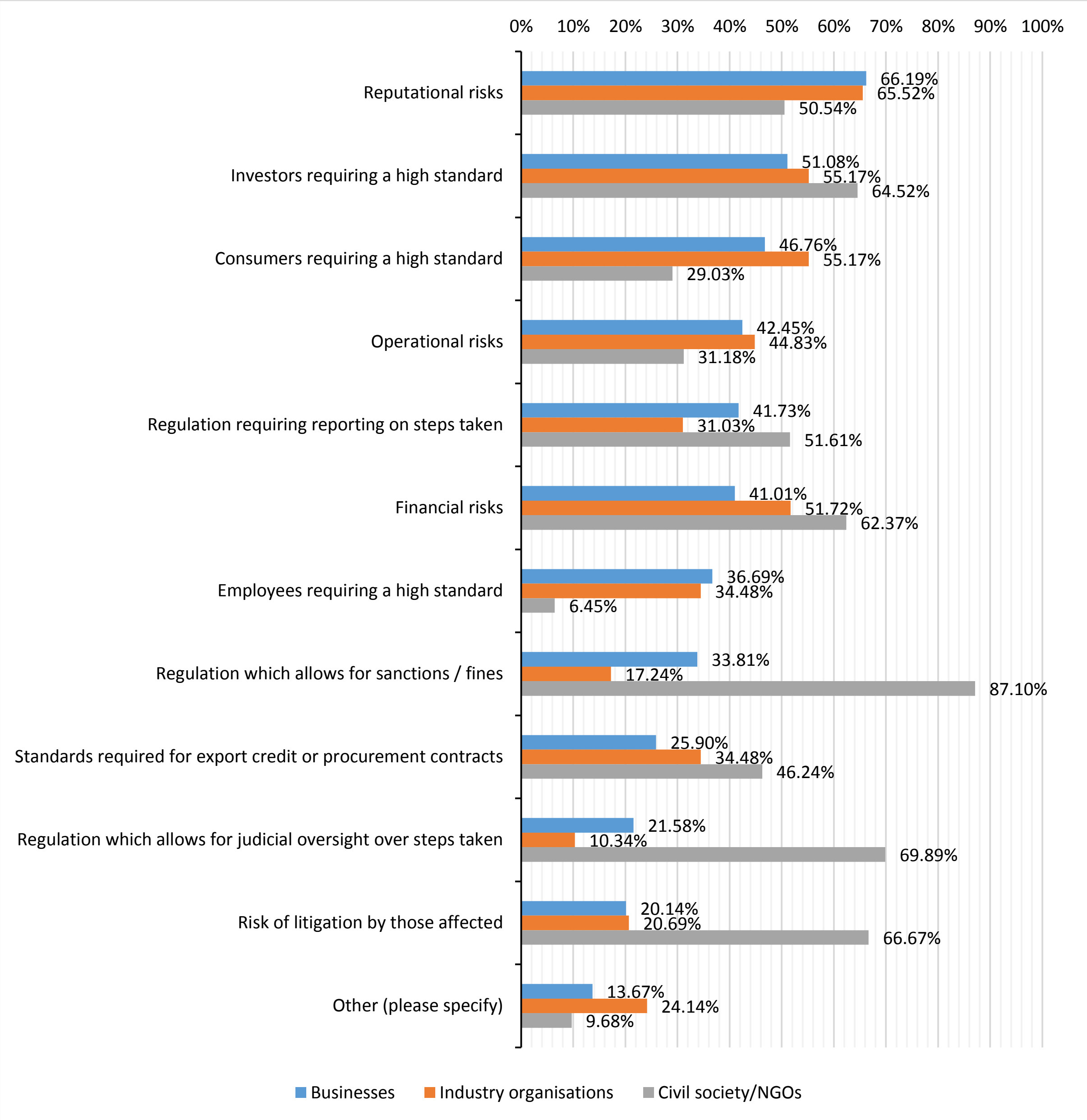
The four least selected incentives by business respondents were (from highest to lowest) regulation which allows for sanctions or fines (33.81%), standards required for export credit or procurement contracts (25.90%), regulation which allows for judicial oversight over steps taken (21.58%) and risk of litigation by those affected (20.14%). It is notable that these are the incentives related to regulation or legal requirements.

Industry organisations placed a similarly low value on the ability of regulatory measures to incentivize due diligence: The bottom four selected incentives by industry organisations were regulation requiring reporting on steps taken (31.03%), risk of litigation by those affected (20.69%), regulation which allows for sanctions / fines (17.24%) and regulation which allows for judicial oversight over steps taken (10.34%).

In contrast, more than two thirds (67.86%) of general respondents viewed regulation which allows for sanctions or fines as the highest incentive for companies to undertake due diligence. This was followed by investors requiring a high standard (62.50%), financial risks (60.71%), reputational risks (58.33%). Thereafter, the other legal-related incentives followed: risks of litigation by those affected (53.57%), regulation which allows for judicial oversight over steps taken (52.38%), regulation requiring reporting on steps taken (48.21%) and standards required for export credit or procurement contracts (45.83%). This was followed by consumers requiring a high standard (36.31%) and operational risks (35.12%). General survey respondents viewed the least likely incentives for companies to undertake to due diligence to be employees requiring a high standard (16.67%).

Civil society stakeholders have a particularly high view of the value of regulation to incentivize due diligence: As many as 87.10% selected regulation which allows for sanctions or fines as the top incentive, followed by regulation which allows for judicial oversight over steps taken (69.89%), and risk of litigation by those affected (66.67%). This is followed by investors requiring a high standard (64.52%), financial risk (62.37%)

and regulation requiring reporting on steps taken (51.61%). Reputation risk was selected by only 50.54% of civil society stakeholders, despite being the top incentive for both business and industry organisation respondents.



Q16 Business Survey; 139 responses – Q13 Stakeholder Survey; 168 responses.

It is notable that business and general survey respondents, particularly civil society respondents, have such contrasting views on what the incentives are, or have been, for companies to undertake due diligence. Business respondents and those from industry organisations, regulation or litigation risks ranked these as lowest of all the incentives (apart from regulation which requires reporting in the case of business respondents). This may be because, for the most part, these legal risks do not currently exist, and respondents were asked about current or past incentives.

In contrast, general stakeholders have rated the legal incentives as the highest. Given the stated purpose of the survey, it is likely that general survey respondents, and in particular civil society stakeholders who are campaigning for or supporting mandatory due diligence, may have answered the question with respect to anticipated future incentives. As such, general stakeholders placed a much higher value on the importance of regulation to incentivize due diligence than business do.

Where regulation is not binding or enforced, such as voluntary initiatives or reporting requirements, they are often primarily aimed at incentivizing companies through reputational risks. The above statistics highlight the importance of reputation risk for companies. However, interviewees highlighted the limitations of reputational risk as an incentive for due diligence. One interviewee from an international civil society organisation indicated:

> [Reputational pressure] only works for companies that are consumer-faced. And there are a lot of companies that nobody knows of, basically. Either they are intermediaries, so people don't really know the name of the companies, or they work in public procurement or in the public sector, or they supply for example retailers. So their own names never appear, so consumers don't know them. So it's difficult to put public pressure on them. That's why we think mandatory regulation would be really helpful.

Another risk of relying on reputation incentives is that due diligence efforts in reaction to scandals, or potential scandals, are focus only on those aspects which are, or may be, exposed in the public domain, potentially overlooking more severe risks which remain unseen. One interviewee from an international organisation which focuses on child labour indicated that:

> If you look at cocoa as an industry, the biggest concern has always been around child labour, at least for the last 20 years. The key human rights due diligence elements focus on child labour. And recently another element of due diligence was related to the environmental impacts linked to deforestation. How they started? Both in reaction to scandals.

The interviewee added that:

> Normally due diligence [...] is mostly driven by either scandals, lawsuits or other legal issues that they have in importing countries if the end consumers are particularly active. This has been brought to life in a responsive way… If you observe companies' behaviour, it has been: 'Okay let's do at least something minimal to react, to show that we do have something in place, so to start counterbalancing, or kind of being protected against some of the criticisms that we have been receiving from the media and from consumers'.

4.13 Digital technologies

It has been proposed that the use of digital technologies could assist business with their supply chain due diligence, and also reduce costs. Accordingly, survey respondents were asked about their use of digital technologies for supply chain due diligence. This is discussed in the section assessing the potential impacts of the regulatory options and will not be repeated here.

Nevertheless, one company interviewee indicated that they increasingly explored the use of technologies, including digital payments and worker surveys, and that they are in the process of developing an internal app:

> We have now the capabilities to go to the worker directly, to ask the worker what do you feel, what do you need. And something the methods that we have is actually quite old fashioned. So this for us is something is going to happen more.

One interviewee working within the government of a large Member State indicated:

> This technology aspect can be a door opener to getting a forward-driven discussion on this, by saying [it is, for example, part of the] EU research agenda, the kind of research we promote. Having a mandatory due diligence law might lead to the effect that we have more funds for research and development channelled into this field. And that suddenly we might find new technological approaches, which really improve the way we manage supply chains in a social perspective. So far, we have not yet invested enough into new innovative approaches. With this technological view, we could try to link our human rights agenda to an industrial innovation agenda, with the innovation objective of promoting human rights. There is not enough on this.

4.14 Overall views on current due diligence practices

General survey respondents were asked in which way do they consider that current due diligence practices fall short. Although this question was optional, it was answered by 144 respondents. Many of these were lengthy and detailed answers, and could not all be set out here. Some comments are listed below, and a larger selection of comments are listed in PART IV: Annexure A.

The general conclusion is that general stakeholders are of the view that current due diligence practices are significantly insufficient to address human rights and environmental impacts.

- "…For many companies human rights due diligence amounts, at best, to reporting." [Further elaboration in Annexure A]

- "By relying almost exclusively on audits and private certification for compliance despite ample evidence of their shortcomings."

- "Risk analysis often focused on supply chain rather than entire value chain effectiveness of grievance mechanisms as a major challenge: especially for third parties/potentially affected understanding the difference between traditional "risk management" (risk to the company) as opposed to human rights risk management (risk to the people) understanding the difference between traditional (legal) due diligence processes and "human rights due diligence"/"responsible business conduct" in line with the UNGPs/OECD Guidance prioritization of issues (e.g. according to severity) identification of leverage and appropriate measures (what can I do if I have little influence?)"

- "I would say in almost every aspect. Companies are not legally required to exercise due diligence, so mainly any company that voluntarily decides to do so applies its own notions and considerations of what a due diligence process should be. This most of the time leads to non- effective mechanisms and activities that just serve to comply with reputational criteria."

- "Current company practices for due diligence are often gender-blind and as such fall short of identifying the specific risks and differentiated impacts faced by women across a company's operations or supply chains. This is a key gap, as there is mounting evidence of the disproportionate and different ways that women are impacted by business activities…" [Further elaboration in Annexure A]

- "Process instead of impact oriented. It's done by a separate silo inside the company, not very much on the radar of the commercial decision makers and therefore all too often not guiding actual business decisions. Often poorly executed, by consultants, and then cherry picked for their implications."

- "In general, my perception is that many SMEs and small mid-cap companies have a very low level of focus and awareness on human rights and environmental aspects of their industry"

- Due diligence not applied across all operations and across the entire value chain (beyond tier one supplier). Often lack meaningful engagement and consultation with rights-holders.

- "Companies lack knowledge of their complex and fragmented supply chains. Even though risks may be identified, they lack knowledge/skills/expertise to address these. In many cases, given that they have thousands of suppliers, they are able to perform DD only on a few. DD usually means audits and reports but not addressing risks."

- "Due to the lack of mandatory requirements, some companies lack due diligence processes. For the ones that have due diligence processes in place, social and human rights are most of the time covered, but the environment component is often the most absent; the climate change component (in terms of emissions reductions) is often there, but not as regards biodiversity, environment footprint mitigation (e.g. deforestation)."

- "Mainly the need to prioritise, based on salient impacts, rather than tackle everything at the same time"

- "Too much focus on reporting and audits and too little implementation and actual engagement throughout the value chain. Sometimes engagement but then purchasing practices fall short of standards."

5. Stakeholder views on impacts of regulatory options

Our surveys asked questions about the likely impacts of the possible regulatory options set out in the Problem Analysis and Regulatory Options below. The views of stakeholders collected during our surveys and interviews will be set out here with respect to each of the regulatory options put to the survey respondents. These findings will be further discussed in the assessment of regulatory options below.

The business survey asked respondents within companies about estimated costs and benefits of each regulatory option. Both business and other stakeholder survey respondents were asked about the sustainability impacts of the various regulatory options. Sustainability impacts were categorized as social, environmental and human rights impacts. The costs and benefits findings are discussed in detail in the assessment of regulatory options, and will not be included here.

5.1 Option 1: No policy change (baseline scenario)

Ten years ago, there were very few domestic-level regulations requiring companies to report on their human rights and environmental risks and implement human rights and environmental due diligence processes.[312] Over the past few years, governments have increasingly been embedding reporting and due diligence requirements into regulatory provisions. The current legal framework applicable in the EU generally, and in various Member States is described in the Regulatory Review section. For the purposes of this

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[312] GBI and Clifford Chance, "Business and Human Rights: Navigating a Changing Legal Landscape", (9 March 2019), available at: https://www.cliffordchance.com/briefings/2019/03/business_and_humanrightsnavigatingachangin.html at 3.

section, it is noted that there is currently no general legal standard which requires companies to undertake substantive due diligence at EU level.
Survey respondents were asked for their views on the current regulatory landscape. They were asked whether they agreed, disagreed or did not know about certain statement relating to the effectiveness, efficiency, coherence of and legal certainty provided by the current legal landscape.

Overall, the majority of stakeholders interviewed and surveyed considered existing laws on due diligence requirements for human rights and environmental impacts not to be effective, efficient and coherent.

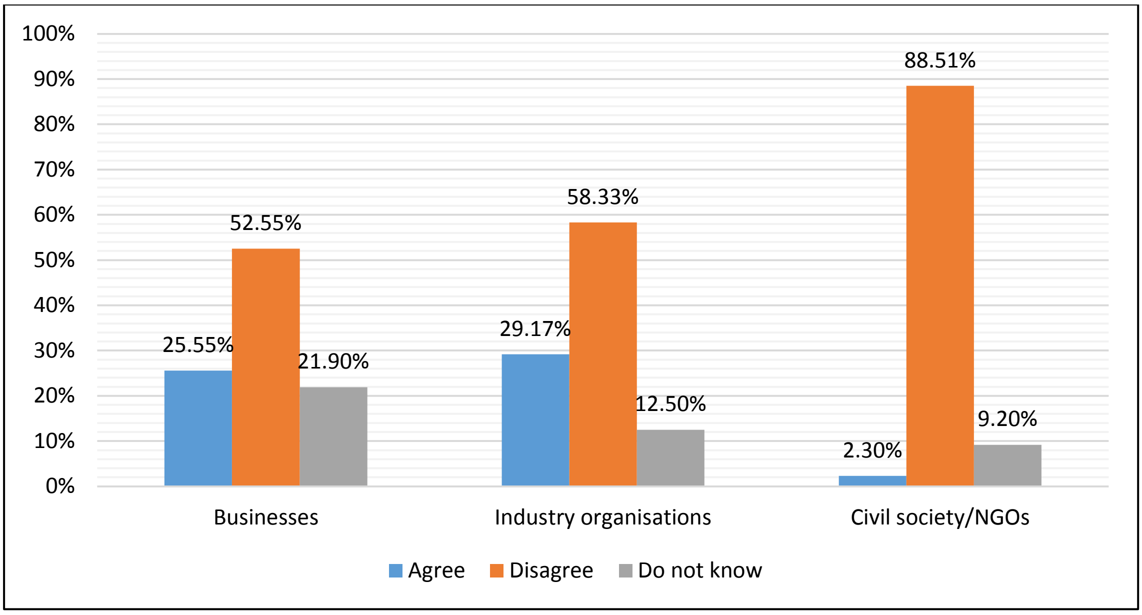
The majority (52.55%) of business survey respondents indicated that, in their view, existing laws on due diligence requirements for human rights and environmental impacts through the supply chain are not effective, efficient and coherent. Less than half of this number, and only 25.55% of business respondents, felt that existing laws were effective, efficient and coherent. The remainder did not know.

Similar trends were reflected amongst large business respondents with over 1000 employees, 53.06% of which disagreed and 27.55% agreed that existing laws on due diligence requirements for human rights and environmental impacts through the supply chain are effective, efficient and coherent. The remaining 19.39% did not know.

Amongst SME survey respondents with 9 employees or less, 28.57% disagreed that current laws are effective, efficient and coherent, and 14.29% agreed, with over half (57.14%) indicating that they did not know.

For contrast, general survey respondents were posed the same question. Overall, they expressed a similar but even stronger view, in that 81.05% of general survey respondents indicating that existing laws on due diligence for human rights and environmental impacts are not effective, efficient and coherent. Only 8.5% agreed with the statement that existing laws are effective, efficient and coherent.

When broken down according to stakeholder group, there is a marked difference between the responses from civil society respondents and industry organisations. Whereas both groups agreed that existing laws are not effective, efficient and coherent, this view was expressed by 88.51% of civil society in contrast to 58.33% of industry organisations. In contrast, almost a third of industry organisations (29.17%) agreed that existing laws are effective, efficient and coherent, when only 2.3% of civil society organisations shared this view. The remaining 9.20% of civil society and 12.5% of industry organisation respondents did not know.



Q17 Business Survey; 137 responses - Q17 Stakeholder Survey; 153 responses.

One interviewee from civil society agreed that the existing framework was not effective, efficient and coherent, explaining:

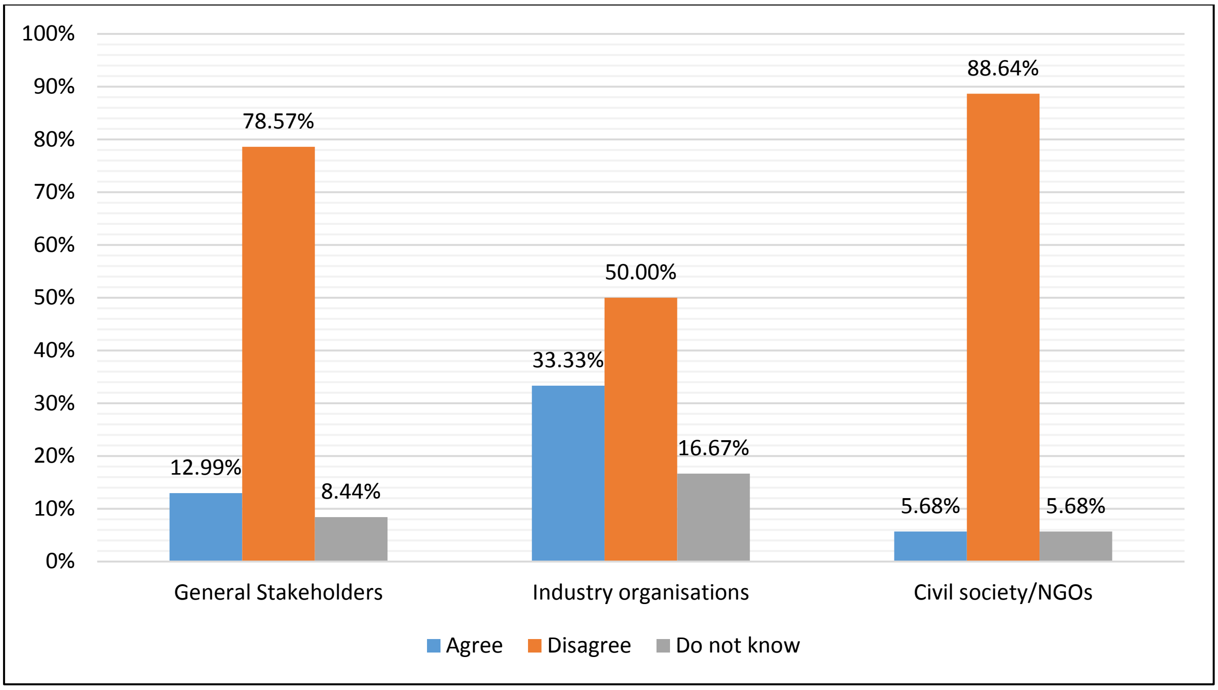
> The coherence is not too bad, but effective and efficient not really. The non-financial reporting directive coherence, the elements that companies have to report on is quite helpful. But if we think back to the environmental side, there are now lots of different regulations and there is a risk there that things just become fragmented. I am sure business have said to you that actually we feel like there are more and more requirements on us, and they don't fit together, they are all slightly different. So something that harmonises that would be useful for everyone.

Another interviewee with expertise in business and human rights in Germany also highlighted the incoherence of a sector- or commodity-specific approach:

> We don't know yet whether the scheme of approved certifiers actually works out well. There is for example a restriction on four minerals. You can ask why those four? And we see a growing number of other minerals that are getting more and more important. Is that coherent? I don't think so.

General survey respondents were also asked whether they agreed or disagreed that, or did not know whether, the current legal landscape provided companies with legal certainty about their human rights and environmental due diligence obligations.

The majority of general survey respondents (78.57%) indicated that the current legal landscape does not provide companies with legal certainty about their human rights and environmental due diligence obligations. However, the views of civil society respondents and industry organisation respondents are notably different in this respect. Whereas both groups view current laws as not providing legal certainty, 88.64% of civil society respondents were of this view, in contrast to only 50% of industry organisations. In turn, only 5.68% of civil society respondents agreed that existing laws do provide legal certainty, a view which is shared by as many as a third (33.33%) of industry organisation respondents. The remaining 5.68% of civil society respondents and 16.67% of industry organisation respondents do not know.



Q16 Stakeholder Survey; 154 general respondents.

A survey respondent from a trade union organisation elaborated:

> The current legal framework does not provide businesses with legal certainty because the *status quo* (i.e. no European regulation and only few national legal frameworks – often sectorial and not effective) is linked with fragmentation and with an uneven playing field in the single market.

One industry organisation with over 16 000 members responded in the survey that their reason for disagreeing that existing laws provide business with legal certainty is as follows:

> EU -companies are doing extremely well and a lot in order to make sure that human rights are not violated in the companies they do business with. Now we need to really obligate those subcontractor -companies to conduct their business according to the standards they are obligated to. As our answer "disagree" to this question…comes from the view that EU -companies at the end cannot feel absolutely safe and certain on their human rights and environmental due diligence obligations, because the different actors at the value chain / end level subcontractors cannot be efficiently obligated to comply with the standards. Even [when] there are third party evaluations and screenings and different audits on these issues, still the subcontractors would need to be obligated more heavily to comply with human rights obligations. Surely there are many subcontractors that are performing very well in practice, but in general the big picture is as described.

As evidenced from the Regulatory Review, the existing regulatory frameworks within different Member States are different. Similarly, and perhaps as a result, companies operating within different Member States are frequently at very different stages of their so-called “business and human rights journey”. For example, one interviewee from a civil society organisation which works with business in Poland indicated that:

> The level of awareness that companies have of the necessity to do something in this area is very limited….More generally this topic is still very new [in Poland].

As indicated above, stakeholders reported that, despite the existing requirements, current company practices for human rights and environmental due diligence in their own operations or throughout their supply or value chains fall short in various ways.

Nevertheless, it was felt that the recent legal developments on due diligence have been useful in terms of driving business practice and focusing attention on human rights issues. One interviewee which advises business on their due diligence indicated:

> I think the one thing that has been the strongest social impact is maybe boosting people's awareness of some of the discussions on the responsible business space. Everyone is now broadly aware that modern slavery is an issue. It wouldn't have been the case before these laws were introduced. It's more on people's radar and that seems like a useful thing…. Too few people are doing proper human rights impact assessments, not at the corporate level but at the granular level. There are some companies that do this very well and very consistently. But they are a lot of companies are finding that really hard, which is partly a resource issue and partly figuring out where to prioritize and where to start.

Most interviewees were in principle in favour of a policy change to introduce a general standard at the EU level, although they differed on aspects of liability and methods of enforcement. The level playing field and legal certainty were amongst the most important considerations for business interviewees, whereas general interviewees highlighted the lack of access to remedies and poor levels of corporate implementation of due diligence.

However, it is noted that industry organisation survey respondents were generally not in favour of the introduction of new policy changes, including mandatory due diligence. It was noted that various steps have already been made in terms of voluntary guidelines and other existing requirements. These more detailed findings will be discussed in relation to key questions below, and contrasted where relevant where the responses of multinational companies.

One interviewee working for a large trade association in the Netherlands indicated that: "Multinationals are now requesting unified rules, as they do not want to be involved in all kinds of national agreements." Another interviewee working for a financial institution mentioned, amongst the benefits of legislation, that "sometimes it helps to get things done, it gives you a push in the right direction".

One interviewee working with the government of a large Member State indicated:

> In general there is a feeling in [my country's] government that some kind of harmonised or unified EU approach and progress on due diligence is something that we need, so no policy change is certainly not a good option for us.

One interviewee working for a commerce association in a Member State where there is currently a campaign, which is supported by business, for mandatory human rights and environmental due diligence:

> No policy change is not really an option after hearing our companies. Something needs to be done. That's quite clear.

5.2 Option 2: New voluntary guidelines / guidance

All interviewees across business and other stakeholders agreed that there is already enough voluntary guidance in existence. However, it is noted that the majority of survey respondents from industry organisations had a preference for voluntary guidelines as regulatory option, drawing attention to the influential nature of those soft law mechanisms already in existence.

One interviewee, who advises companies on their due diligence, indicated:

> I'm just not sure what a regional document would add to the UN Guiding Principles. Fragmenting attention away from an international standards is just confusing to people.

An interviewee from an international civil society organisation summarized the general position of stakeholders concisely:

> There is enough documentation that voluntary standards have not brought the change that we need. The majority of business are not discharging their responsibility towards human rights.

Similarly, survey respondents overall seemed unconvinced that new voluntary guidance would have notable social, environmental and human rights impacts. When asked whether new voluntary guidance would have social impacts, business respondents were fairly evenly split, with 40.71% indicating that it may have social impacts, and 35.40% that it is unlikely to have social impacts. Business respondents indicated by 41.07% that new voluntary guidance is unlikely to have environmental impacts, with 33.93% indicating that it may. Similarly, a greater number of business respondents (40%) indicated that new voluntary guidance is unlikely to have human rights impacts, with 38.18% indicating that it may.

General survey respondents were even more dismissive of the likely impacts of new voluntary guidance. Over two thirds (67.11%) indicated that new voluntary guidelines will not have social impacts,[313] even more (68.46%) believed that it would not have any environmental impacts,[314] and similarly, 68.46% thought that it is unlikely to have human rights impacts.[315]

Interviewees indicated that voluntary guidance could be helpful to supplement any legal obligations. For a further discussion on the role of non-binding guidance to accompany a binding legal standard, see the Problem Analysis and Regulatory Options section.

One interviewee from a civil society organisation indicated that:

> We have been in a situation where there has been plenty of voluntary guidelines for a number of years and we still have way more human rights violations in the global value chains than we should.

Another interviewee from civil society stated that:

> There is an abundance of evidence that the voluntary mechanisms are not working sufficiently. Looking across a wide-range of sectors, you get this conclusion that the current state of affairs of due diligence, based on the largely voluntary implementation mechanisms that are there, leads to a quite ad hoc, unsystematic, in general relatively low uptake of due diligence processes.

The interviewee added:

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[313] Contrasted with 25.5% of general survey respondents who thought that new voluntary guidance may have social impacts.
[314] Contrasted with 18.79% of general survey respondents who thought that new voluntary guidance may have environmental impacts.
[315] Contrasted with 22.15% of general survey respondents who thought that new voluntary guidance may have human rights impacts.

> It's now 8 years or so since the normative expectation of due diligence came into play with the Guiding Principles and the OECD Guidelines. Obviously there's a bit of a grace period for people to get adjusted but the pace of take up is just far, far, far too low and the way it's been taken up is very much ad hoc and not structural and I think that that does indicate that if we want companies to take this seriously we need to move towards more legislative and regulatory forms of expecting them to do so.

Another interviewee from civil society indicated that:

> The voluntary guidelines have not delivered in practice…I wouldn't go for more guidance, because it's not about the guidance, it's about doing it, actually.

Several interviewees also highlighted that, due to the nature of due diligence, existing voluntary guidance will influence the standard of due diligence that would be expected of companies under each specific circumstance. For example, one interviewee indicated:

> I think there are already enough guidance on which to base an understanding of the scope of due diligence. Not only the UNGPs, but the OECD guidance and all the guidelines on specific sectors too. I think this would be [what] a judge may refer to.

One interviewee from an environmental NGO mentioned, with regard to deforestation, that:

> One of the problems is that not all companies have taken on 'no deforestation' commitments. Some of the more publically exposed ones ... may have taken on zero-deforestation commitments, but then others who are less publically exposed ... or traders that nobody has heard about, but that are hugely profitable and significant actors in the value chain ... they are less likely to even make a commitment in the first place or to be conducting due diligence on a voluntary basis ... There is a problem of free-riders, the majority of the market is not taking on voluntary due diligence and it's just a few that are publically exposed actors that are doing that.
>
> The other problem is that in practice, even when companies make commitments, they aren't enforcing them. There is no accountability for failure to meet a, for example, zero-deforestation commitment.

5.3 Option 3: New regulation requiring due diligence reporting

The third option for consideration is new regulation requiring companies to report on their due diligence. It is noted that unlike mandatory human rights and environmental due diligence duties, which are still rare, various existing laws already require some form of reporting on due diligence for human rights and environmental impacts.

However, existing reporting laws do not currently require, by way of law, compliance with the first three components of due diligence (identification and assessment, taking actions to address, and tracking effectiveness). Most existing laws are also currently not enforced by way of sanction for a failure to report.[316] These existing laws are discussed in more detail in the Regulatory Review, but it should be borne in mind that experiences

[316] Some examples exist in the English system where companies have been fined for shortcomings in their reports. See the UK country report in section 3 Regulatory Review.

with these laws have expressly informed survey respondents and interviewees responses discussed below.

Survey respondents were asked whether new regulation requiring due diligence reporting would be likely to have social, environmental or human rights impacts. Here, survey respondents were more positive about the likely impacts than with new voluntary guidance.

The majority (50.47%) of business survey respondents indicated that new reporting requirements would have social impacts,[317] and 40.9% that it would have impacts on the environment.[318] A slightly larger majority (55.24%) of business respondents indicated that new regulation requiring due diligence reporting would have impacts on human rights, which contrasted with only 18.10% who indicated that it would not.

Similarly, the majority (52.03%) of general survey respondents indicated that new reporting requirements on due diligence would have social impacts.[319] General respondents were more evenly split on whether it would have environmental impacts, with 44.59% indicating that it would, and 39.19% that it would not. Similarly, 47.97% of general respondents indicated that new reporting requirements on due diligence are likely to have human rights impacts, whereas 39.86% believes that it would not.

The figures regarding the likely sustainability impacts of new reporting requirements are rather high, particularly given the existence of the EU non-financial reporting directive which already requires reporting on due diligence process. Moreover, these views on the potential impacts seem to be high in light of the perceptions about the limitations of reporting requirements which were expressed frequently by interviewees and survey respondents across business and other stakeholders.

Various regulatory reviews and civil society reports, which are set out in the Regulatory Review section, have highlighted that existing reporting requirements have led to low levels of reporting and poor quality of reports. Our interviewees confirmed these shortcomings of reporting requirements, from their experience. Most had strong views regarding the limitations of reporting requirements.

The following explanation by an interviewee from an international civil society organisation summarises the general views of interviewees:

> The [EU] non-financial reporting directive is not at all a context in which adequate due diligence could be actually regulated or encouraged. Because it is an annual report of managers in the context of accounting. When you look at reporting on due diligence there is much more than needs to be done. Not only whether it has been done, not only outputs, or so. I mean, there is a lot of information that needs to be disclosed anyway to enable and empower stakeholders to engage in the identifying [and] mitigating process. That's the one thing.
>
> The other thing is, as a concept as such, we urgently need definitions of the standard of care. A [law] imposing what the standard of care is. And if you regulate reporting and disclosure, you just don't do it. I mean, you indirectly hope to trigger certain processes and to trigger due diligence, but what we need at the moment is: What is the standard of care? That needs to be defined…You need processes in courts or through authorities actually to concretise the standards of care. We need access to remedy. And this would all not be feasible with a requirement to disclose because there the obligation is the disclosure. And

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[317] Contrasted with 22.43% of business respondents which indicated that new reporting requirements on due diligence are unlikely to have social impacts.
[318] Contrasted with 32.38% of business respondents which indicated that new reporting requirements on due diligence are unlikely to have environmental impacts.
[319] Contrasted with 37.84% of general respondents which indicated that new reporting requirements on due diligence are unlikely to have social impacts.

> sanctions [there] are linked to disclosure and not to standard of care, or harm, and that's what we actually need.

Stakeholders noted that because reporting requirements rarely provide for a sanction in the case of a failure to report, they have been shown to result in low levels or reporting, and low quality reports. For example, interviewee from an international trade association who works with companies on their due diligence indicated:

> [The UK Modern Slavery Act] has proven partly effective in terms of transparency. We know there are many thousands of companies who are not adhering to the non-slavery act in the UK, for example, but we ignored it. There's very limited enforcement of that law by the UK government … I think it's a real limited value. It does not allow consumers to really interrogate whether the supermarket they shop at or the clothing company they buy at are really ethical. They can't determine this. It's too difficult, you can't expect individuals to be able to assess those practice through a one-page glossy CSR statement … [Reports are] very catchy, very inconsistent in terms of what's reported, and how. And lacking quantitative data to really determine that [there are] good measure[s]. No data on wage level for instance.

Similarly, an interviewee from a civil society organisation which has worked on company reporting under the EU non-financial directive stated that:

> The EU non-financial directive establishes a legal duty for companies to disclose their [due diligence] practices. The form of how they are meant to comply with that duty to disclose has not been clarified in that directive. It's the opinion or ours and other NGOs and some companies indeed that it should be specified as the UNGPs human rights due diligence reporting framework. Precisely because it is so clear, and defined and methodologically guiding. It explains to companies how they should identify their human rights risks, with salience rather than materiality being the guiding sort of principle for their business operations and then how best to prevent, mitigate, remedy, etc.

In addition, stakeholders also criticized reporting requirements insofar as they do not require any substantive due diligence to take place. An interviewee explained that "[i]t doesn't make sense to require companies to report on something that they are not required to do."

Similarly, another interviewee from a civil society organisation referred to the implementation of the UK Modern Slavery Act, that:

> Only with transparency requirements, you don't really drive change. You don't really achieve real change…[L]ooking at the implementation of the UK Modern Slavery Act transparency in supply chains provision, the result that we are seeing is that companies are only required to disclose their efforts to combat human trafficking. They are only required to disclose what they do in case they do something. But if they don't do anything at all, actually there are no real consequences. So the fact that you give these comply or explain options to companies means that at the end they are not required to undertake any kind of real action.

A co-interviewee from the same organisation added, with reference to the EU Non-Financial Directive, that reporting requirements tend to focus on the provision of information to shareholders and investors:

> Reporting requirements in and of themselves do not stimulate change in corporate behaviour. That's acknowledged in numerous literature studies. We see in the discussions with the NFR and the like that it's really intended as giving information to investors. Which is an altogether different policy objective as to change corporate behaviour. It's really about letting investors know where the

> most ethical behaviour is, where they can move their money, which is an altogether different policy objective to ensuring a proper response in terms of conduct let alone access to justice for victims.

Another interviewee from an international trade association highlighted that:

> [T]ransparency is not an end into itself. In that, you could force companies to disclose more information. It does not automatically lead to improved conditions in the supply chain.

One interviewee working within the government of a large Member State where a due diligence law is being considered indicated that:

> We hear from the UK Modern Slavery Act that it seems to be not very effective because it is a mere reporting exercise with no state control to it, but it's rather left to the civil society like NGOs to make use of this information. It seems that there is a growing disenchantment with the effect of this. Also, companies learned how to use it and deal with it, so now there is professional industry that delivers the right statements, there's a large feeling that they become hollow.

Interviewees across business and other stakeholders agreed that new reporting requirements on due diligence would not be desirable. One interviewee from a transnational company indicated:

> Making it mandatory for companies to say whether they are doing something or not is not enough, companies should have to do something.

Similarly, an interviewee from civil society suggested that new regulation should go beyond requiring reporting:

> There is already really a plethora of these reporting requirements. And what we have seen is that literally a handful of companies put out meaningful information, and then use that to reflect on the way they do business. If all that you have to do is report, you don't have to actually to do anything. And you can report that you have done nothing and that is an adequate report…I do think more reporting is not going to drive changes in practice.

The interviewee added:

> With reporting, companies all look around to see what somebody else is doing…'Ok so someone has written a three page report, so we'll do that as well.' The theory about reporting is that it drives a race to the top. I think in fact it drives a race to the middle. Companies will say - I have had people say this to me – 'Oh, we came out in this ranking, we were about 40%. Our CEO said: Well I don't really like that, where's everyone else at? They're all at about 60. So what do we need to do to get ourselves up to 60?' Not 100. I think we need to factor that kind of thing in.

It was noted by more than one interviewee that there is also a risk of unintended adverse consequences if reporting is the end goal of the legal requirement, as companies may be taking important but sensitive steps as part of their due diligence, about which they should rather not be reporting. One interviewee from civil society indicated:

> Companies might not be reporting on everything they are doing, because it's kind of sensitive, involved negotiations with unions, or there is some kind of issue where you maybe do not want to publicize it, perhaps it's around sexual abuse, there is a risk to the people involved.

This risk of a disproportionate legislative focus on the reporting component of the due diligence process was confirmed by an interviewee from a multinational food and drinks company:

> I think we need to be careful to avoid generating unintended consequences. Because in our experience when we engage not only with our people in the markets, in the country operations, but also suppliers, business partners, and also stakeholders like NGOs … based in these countries. One thing that really helps us get to the bottom of the issues that we are looking at as part of human rights impact assessments is…the kind of confidential nature of the human rights impact assessments.
>
> And I am saying that because it is a very different exercise, I think, when you carry out some sort of human rights impact assessment, when it is confidential and when it is not. Basically…the kind of results you will get are different. Because the confidence of people to share that with you is different. And there is a risk that if, from the beginning, if you actually make this process fully open and transparent, then you basically commit or have to disclose all the results and findings. There is huge risk that you won't actually get to the bottom of things. And one of the objectives of any law, and this law in particular, should actually be to improve the situation on the ground. And I fear that if we go for too much disclosure requirements, this is not what we will achieve.
>
> Now, having said that, there is still of course a lot of room for openness, transparency and disclosure, but maybe not that much in terms of the findings, but more in terms of the action plan, so the remediation action. And I think that is a huge difference. Because then it is also allows companies to focus on things they commit to improving based on risks but without having to disclose them.

One interviewee also highlighted that law which only requires reporting, but not the other components of due diligence, tends to focus on listing or quantifying the steps taken, but do not focus on the actual effectiveness of steps taken. An interviewee who works with businesses in the implementation of the UNGPs stated that reporting - the fourth components of due diligence - is less meaningful if it not accompanied by the tracking of effectiveness - the third component of due diligence:

> I think the other area that businesses find very challenging is the third step of due diligence which is tracking. How do you actually know if what you're doing is leading in any way to better outcomes for people, rather than simply measuring the activities that you're conducting as a business? So the number of audits, the number of staff trained, the number of suppliers with policy commitments, the numbers of contracts signed that include a supplier code of conduct. (...) I can't do very much with those metrics in terms of gaining confidence that the measures the business is taking are moving in the direction of better outcomes for people.

Another interviewee from an international civil society organisation indicated:

> Reporting is an important part of due diligence…but reporting needs to be done in the context of a larger normative framework that obliges companies to do due diligence effectively to put in measures in place to prevent harm…It's the showing what they've done. Showing the public in general what they have done to prevent harms. So I think it is important but it cannot be and it will never be the way in which you will tackle the problem, in the absence of everything else that is needed.

One interviewee from civil society indicated:

> One of the lessons from the UK Modern Slavery Act, is just reporting what you have done does not take you very far. And that reporting needs to evolve to be

> around the effectiveness of what you have done, so that reporting is a lot more reflective, rather than just you listing off well we've put in place a load of policies.

They further indicated that standardised performance indicators to measure effectiveness would "evolve over time, rather than something that you could put in place from the very beginning."

In relations to child labour, an interviewee working for an international NGO indicated that:

> A side effect of interpreting due diligence obligations as meaning: 'Ok, I need to monitor, I need to be able to account or report how many children are in my supply chain', is that it came with an insane amount of money spent on very little value added actions, and very little money spent on what can actually change life of people which is remediation.

However, views on reporting requirements are not all negative. On the contrary, it was highlighted by several interviewees that reporting requirements such as the EU non-financial reporting directive have had a positive impact on the internal conversations taking place within companies. One interviewee from a transnational company based in Spain indicated as follows:

> [The implementation of the EU non-financial reporting directive in Spain] has really impacted in the company. For me, particularly, I could not be happier. We have always felt the support of the company. But some other areas of the company, they do understand when something happens, but they do not really understand how far this is also affecting the rest of the business model. When you wrote to your colleagues, and you talk about materiality analysis, when you talk about GRI standards, when you talk about reporting, when you talk about transparency, when you talk about traceability. They listen, but you take care of it. And now the conversation is all over the company. I have people from other departments: Can you come to my office and explain to me this thing about materiality that you have been telling me for many years? Because we have already been doing it, for me it's being great, because now we have the back-up of something as big as the European Union and all the lawyers are now behind it, so it really helped. I have seen other departments in my company really going crazy trying to get all the information that we need to report. Humbly, I had it in five minutes. Because this is the data that I manage. I did not have to create anything. They were asking how many factories do you have and I have it here because I have a system and I just have to press one key. This is something that is giving another level of visibility within the company. For me, these types of laws, that even if they are only saying say what you are doing, are very relevant.

One interviewee working for a financial institution explained that the UK Modern Slavery Act has had some effects in terms of bringing some "boardroom awareness, because people have to put their signatures", but not as having affected corporate practice. A co-interviewee working in the same institution explained that:

> It provided the opportunity to put this on the agenda of the managing board. The statement contains no new initiatives or information. It is only a summary of what we were already doing within different roles of the bank, and specifically on modern slavery. However, when we sent the memo and the draft statement to the bank, I think they came back twice with some sort of requests for more information about how certain procedures worked or why we chose certain language. So it sparked some interest on the topic which was perhaps not there before. But then again, as soon as it got approved that was it. There wasn't any follow up or changes or increase in level of ambitions. We are quite ambitious,

specifically on this issue, but it is not because of the Modern Slavery Act requirements.

A company interviewee also highlighted the role of the UK Modern Slavery requirement in providing the language for companies to speak about their impacts:

> It made us more comparable within brands, because we could be speaking about different things, and they were true and they were relevant, but if you use the data in another way or another you may sell what you are doing in a different way. But with the [UK Modern Slavery Act] you were comparing potatoes with potatoes. I mean that's what it was. How far have you gone in your traceability, how many tiers do you know?

5.4 Option 4: Regulation requiring mandatory due diligence as a standard of care

Survey respondents were asked several questions about the impacts and effectiveness of a regulatory option of mandatory due diligence and its various sub-options (set out in the Problem Analysis and Regulatory Review section).

A large majority (65.59%) of business survey respondents indicated that new mandatory due diligence regulation is likely to have social impacts. Only 11.76% disagreed. Regarding environmental impacts, 52.94% of business respondents believed that mandatory due diligence regulation would have impacts on the environment. Moreover, more than two-thirds (67.65%) of business respondents believed that mandatory due diligence would have impacts on human rights. Only 9.8% of business respondents believed that it would not have human rights impacts.

General respondents were even more convinced of the likely impacts of mandatory due diligence requirements. The vast majority (86.39%) indicated that it would have social impacts, contrasted with only 4.08% who disagreed. Again, 81.63% indicated that it would have environmental impacts, and only 4.76% indicated that this is unlikely. Similarly, 86.39% of general respondents believed that mandatory due diligence requirements would have human rights impacts, and only 3.4% believed that this is unlikely.

The majority of the stakeholders interviewed supported the introduction of a general requirement at EU level which would require companies to undertake mandatory due diligence in their own operations and throughout their supply chains. However, interviewees differed with respect to liability and the enforcement method for implementation.

One interviewee from civil society which specializes in corporate accountability across sectors indicated that this kind of regulation "would be a massive step forward, and if adequately crafted it has the potential to make a huge difference." Similarly, a survey respondent from a trade union organisation indicated:

> An effective and ambitious European legislative framework obliging companies to establish due diligence mechanisms for their supply chains is a *conditio sine qua non* to enhance European companies' sustainability and ensure fair competition in the internal market.

One interviewee from a multinational company explained the reasoning behind many multinational companies' support for a due diligence regulation:

> Those benefits would be first and foremost a level-playing field. Having everyone play by the same rules, to reduce complexity and bring some clarity. And, related

to the level-playing field, and maybe the most important reason, is that it would help to drive mainstreaming good practices. Which is important for the sake of our planet and people in our supply chains. But also, more selfishly, because when we're working on a particular issue, when we don't have all the actors along the supply chain at the table caring as much as we do, it's much harder to get to the root of the problem. So you need not just the consumer-facing companies and those who get NGOs campaigns pushing them to do certain things, but you need all the actors along the supply chain to also have good reasons to pay attention and to put the resources towards solving those issues.

An interviewee from a multinational food and drinks company indicated:

> As a company we believe that legislation can give the right incentives for companies to address their human rights so as a principle we would welcome a legislation, potentially one that is covering the entire EU would most probably be preferable than having a patchwork of legislations with different kind of criteria or addressing different kind of issues which is also an issue. But of course, this legislation should really create an enabling environment, and not only focus [either] on a tick-box exercise or on punishment of companies.

Confirming this reasoning by large businesses, one interviewee from an international trade association which advises companies on their due diligence indicated:

> I think a single harmonized, legal standard could be very valuable. I think the businesses we work with would genuinely value that if the legislation of the policy is intelligent. Most businesses we work with are already doing significant amounts of human rights due diligence.

An interviewee from the European Confederation of Directors Institutes ("EcoDa"), similarly confirmed the importance of a basic requirement of care:

> It is fair to say that at Board level these topics are mentioned, and are discussed. The important point is to ensure that these topics, whether it is supply chain, corruption, labour force, human rights, that they are mentioned and tabled on the agenda. So that the Board can say with the executives concerned: Is it a problem in our company? Do we have a policy for it? How to apply our policy? And how far do we go into the reporting, and how frequently? And it can take five minutes in one company; it can take five hours in another.

In turn, civil society stakeholders expressed the view that it is essential for the regulatory mechanism to create remedies for those who are affected:

> In terms of saying what we would like it to look like: A requirement to carry out due diligence in accordance with the Guiding Principles and then enabling provisions that allow people who are adversely affected to hold the European parent companies to account in the home jurisdiction of the parent company.

An interviewee working for a French business organisation indicated that the French Duty of Vigilance Law had already had positive impacts on business practices:

> It forced enterprises to reexamine their current HR practices, and to systematize, formalize and integrate them for all of their activities.
>
> Many companies know their salient human rights issues because they have been challenged by external stakeholders and have to respond to extra-financial agency questionnaires. But perhaps they had not addressed all human rights

issues. Now they have to and they have to prove it, for all the companies and all the subsidiaries in the supply chains.

The interviewee added:

> Around 50% of large companies concerned by the law have a dedicated approach regarding human rights. The other ones only refer to ethical principles or human rights policies (...) but they don't identify their most salient human rights issues so it's not a proper response.
>
> Before the law, only perhaps 20% had this kind of dedicated human rights approach and it was the companies the most challenged by stakeholders because of their sector, country or activity, etc. (...) The law helped some companies to systematized and formalized a dedicated human rights approach at corporate level and integrate it into global processes.

5.4.1 A standard of care rather than a process

Interviewees also highlighted the importance of the use of a standard of care requirement (rather than due diligence as a mere process) as it would require companies to do whatever is required to prevent and mitigate human rights risks, rather than simply create "tick-box" processes.

One company interviewee indicated that it is better to have a regulation for which "you have to show the result and not so much the process":

> Due diligence is a very complex process. I have done a lot of survey and questionnaires for NGOs on due diligence, and sometimes I get really upset. Because I can understand that they get fixated on process. But I may not have artificial big processes with A B C, but I have the results, I have the reality of the supply chain. So how do you differentiate it when you create a due diligence regulation between those people who have created and empty process and those people who may not have super structured formal process, of this goes here and this goes there, but there is actually a lot of information…. When you are really doing things and you do not want to hide, you want questions that can actually show how you are managing your impacts. Not how good you are at creating big processes with arrows.

Concerns were also raised about due diligence being understood as a "tick-box" process. For example, an interviewee from a financial institution indicated:

> The benefit of legislation is that it is easier to put on the agenda of the managing board. It allows you to get more capacity internally. In the financial sector regulations, there are tons of people working on implementing that, and significantly less on the human rights or environmental due diligence part. So mandatory legislation may free up more capacity within companies.
>
> However, the type of people that would be placed into such a job could be made part of the compliance departments, which are interested in complying with the law and nothing more than that. While the people who are usually staffing sustainability departments are in it for different reasons. So they are not merely interested in complying with specific mandatory standards, but are also interested in positive change proactively addressing human rights issues, seeing different connections between initiatives, speaking out on certain issues. And that's not the type of work that compliance do. So if mandatory legislation would shift this whole field towards compliance teams internally, it creates different dynamics

> within companies. And that's what you could be afraid of, in a sense, as a result of legislation.

Similarly, another company interviewee indicated that:

> We do have a different scheme than my colleagues from the legal compliance department. We do put workers at the centre. I want to make lives of the workers better, and of course I want to do that by avoiding risks to my company. … But if the only thing that the regulation is telling me is: 'What is your process for due diligence?' I mean how is the right-holder improving their lives with that? How does it matter if I am meeting with the legal department three times per week to tick some notes? … We should be able to see the whole picture of impacts and then focus on what you find most salient, but [the regulation should focus on] what have you done, what is the final change in the lives of those rights-holders because of your due diligence processes.

An interviewee from a French business organisation indicated:

> A huge challenge today is not to interpret the [French] law in a strictly compliant manner ... but really to understand the law through a continuous improvement approach. And the spirit of the law is the UNGPs and CSR frameworks.

An interviewee working for a French business organisation indicated that the French Duty of Vigilance Law explained that:

> The question of internal actors to implement the law is very crucial (...) There are many different perceptions and understanding of what are the objectives of the law between different internal departments. All departments have to be involved in the implementation of the law because there are human rights issues, environmental issues, health and safety issues and it's not the same internal departments which address all the issues. It [the law] asks for risk-mapping so risk officers have to be involved, there is also monitoring so internal control and audit are involved, and its a law so legal and compliance departments are involved too. We really see a need to have a shared understanding, a shared vision of the law and the objectives of the law. Except for CSR departments, it's very difficult for other departments to understand that the risks to consider are not to companies and the objective [of the law] is not to protect companies but it's only to protect people and the environment

An interviewee who works with businesses in the implementation of the UNGPs stated that:

> What we're always really interested in is how to you drive meaningful behaviour change by business that goes beyond superficial compliance and that goes beyond treating this as: 'Now you've just made human rights another tick-box exercise which we'll treat through templates that law firms will sell to us' and so on and so forth.

5.4.1 A general, context-specific standard

Many stakeholders, including all interviewees, emphasized that the standard of care should be general and flexible so as to take into account the specific context of each specific company. This is consistent with the UNGPs which state that due diligence "[w]ill vary in complexity with the size of the business enterprise, the risk of severe human rights impacts, and the nature and context of its operations."[320]

For example, an interviewee from a multinational food and drinks company who advocated for the regulation to be based on the concept of due diligence contained in the UNGPs explained:

> [T]he amount of due diligence and the level of due diligence that each company will carry out will be different, based on its size, its structure, its business relationships, the risks that it faces. And I don't know how easy / difficult it is for a law to recognise that [in a law]. But this level of flexibility is really essential if we really want to make sure that our suppliers, and you know, some of them are big but a lot of them are really small, can also actually participate in this effort to carry out due diligence and improve things. Because the risks that we face are mainly with these small-size enterprises, and actually to a very large extent, with … farmers themselves … I think this flexibility within the law that we have in the Guiding Principles, it will be great actually to see it in a law at the European level.

The interviewee added that this flexibility provided by the concept of due diligence in the UNGPs also means that a general cross-sectoral mechanism could be applied to all sectors and sizes of companies, as the due diligence test will be for a contextual risk-based approach:

> If the law is flexible enough towards the risk of exposure to business, then we would not actually need sector-specific laws. For example, in our industry we know that the main risks that we face are in the upstream supply chain. So if there is a way for the regulations to [point out] that companies need to actually look at where the risks are, I think you would not need such sector-specific legislation. Because the risk would be different for each sector and each company, but then … that would be the responsibility of [each] company to assess and identify these risks, be they in the upstream supply chain, or be they in the mine, or on a specific site, or in the downstream supply chain, it does not really matter.

A survey respondent from an international industry organisation explained in an optional text box:

> There can be a delicate balance between competing objectives regarding human rights, environment and climate change. Companies frequently face difficult choices while pursuing different objectives. For example, a catering company operating worldwide may want to reduce CO^2 emissions due to transport of food and consequently decide to source food locally. However, local food production may involve farmers whose children participate in the local food production. This is a typical dilemma which companies would not face if local governments applied minimum environmental, social and human rights standards.

An interviewee from a business membership organisation said:

> There is a need for a tailor-made approach, not a one size fits all approach, especially if it is mandatory. Because corporations are so widely different in size, in activities, in history – some are brand new, some are 200 years old – in international position, that thinking that all companies, let's say apart from the very small ones, can apply the same practices and same information, and the same rules is an illusion. It's easy on paper, but it is an illusion.

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[320] UNGP 17(b).

One interviewee from a civil society organisation explained:

> I think it's a really interesting approach. Because what I see also is there are some really obvious cases. Like I went to a conference [and] there was an indigenous woman from Alaska … and she was saying people were killed because they were complaining about their land being taken by oil companies … It was so obvious, and on that I'm like: 'Can't we have a law to prevent that?'. But as soon as you discuss a law for these obvious cases, then all the really complicated cases come up and people say: 'Oh, we can't do it because there are some complicated cases.'
>
> So I think the approach [that] is so general, and would allow for context-specific things, that would allow taking to court those companies that really do gross, direct human rights violations, and at the same time have some room to take [into account] the circumstances for other companies that are not so directly involved, where the issue is more complex. I think that is a really good approach. We can't wait and not do anything about the obvious cases just because there are really complex cases.
>
> For example, on child labour in the cocoa sector, it's really complex. The companies, they don't employ children directly. There are different intermediaries, there is a poverty issue, there is a cultural issue, there is a lack of alternative economic possibilities, I mean, there are so many other factors that you can't really hold a company liable directly. They have to play their own part, but it's really complex. We can't not have a law because of these complex cases and then let the other continue violating human rights.

These arguments also tie in with the views of stakeholders relating to due diligence as a defence, which is discussed in the following subsection.

5.4.2 On due diligence as a defence

Stakeholders across the spectrum highlighted that companies should be able to escape liability if they are able to demonstrate that they have, in fact, undertaken the due diligence required in the circumstances.

As is noted in the Problem Analysis and Regulatory Options section, a legal standard of care which is not a strict or absolute liability (or "no fault" liability) would imply that there would be a defence available to companies to show that they have undertaken the required level of due diligence. There are various examples of where due diligence is used as a defence in current laws or legal proposals, discussed in more detail in the Regulatory Review. Examples include the UK Bribery Act 2010[321] and the Swiss Responsible Business Initiative and counter-proposal.[322] For further elaboration on the test which the due diligence defence could take (for example, "adequate" due diligence, "reasonable" due diligence, and so forth), see Problem Analysis and Regulatory Options.

One interviewee who works with businesses in the implementation of the UNGPs indicated that:

> In the text of the UNGPs, it is clear that conducting [due diligence] should not be an automatic defence. And I think that it's this issue of automaticity that is the

[321] Section 7(3) of the UK Bribery Act 2010 provides a defence to corporate criminal liability if companies can prove that they had in place "adequate procedures" designed to prevent associated persons to engage in bribery.
[322] Article 2(c) of the Swiss Popular Initiative on Responsible Business provides that parent companies are not liable if they can prove that they took all due care to avoid the loss or damage, or that the damage would have occurred even if all due care had been taken. Nicolas Bueno, "The Swiss Popular Initiative on Responsible Business: From Responsibility to Liability", in Liesbeth Enneking et al (eds.), A*ccountability, International Business Operations, and the Law*, London: Routledge (2020), 239.

> problem. And "safe harbour" implies "I do this, snap, I'm free, whatever happens I'm out". And I think that's the issue that then causes an understandably negative reaction from civil society and others, and a lot of concerns.
>
> What we certainly think is reasonable is that in any consideration of liability, the adequacy, the appropriateness of the due diligence that they conducted would be taken into account. That's integral in actually making decisions under the UNGPs about whether a company contributed or not…The adequacy of their due diligence measures helps place them on a spectrum between contribution and linkage.

However, in accordance with the UNGPs, conducting due diligence would not create a "safe harbour" or a "tick-box exercise" whereby companies are automatically absolved from liability. In particular, the commentary to Guiding Principle 17 notes that:

> Conducting appropriate human rights due diligence should help business enterprises address the risk of legal claims against them by showing that they took every reasonable step to avoid involvement with an alleged human right abuse. However, business enterprises conducting such due diligence should not assume that, by itself, this will automatically and fully absolve them from liability for causing or contributing to human rights abuses.

An interviewee from civil society indicated:

> In this debate, the concept of "safe harbour" is not a very helpful concept, because it is mixing things together. From our perspective, we would want to say to companies: It's not in your interest *not* to report. Because if something does emerge, if an issue emerges, or an allegation, it's in your interests to show that you are aware of it, you had identified it, you are dealing with it. And if for whatever reason it had not been resolved, then you have got the information there to say: "Well, we were trying to address it, this is as far as it had gone", whatever the circumstances were.

One interviewee who works with business on their supply chain due diligence highlighted that the law is unlikely to create liability for those companies who are already undertaking comprehensive due diligence. Instead, such a law may benefit such leading businesses by raising the standard in operating contexts where individuals have not been able to create change in their own:

> Even these front running companies, who take this stuff very seriously, are going far beyond. They would not be impacted by this legislation because they are already doing the due diligence. They are not able to foster the conditions that actual decent work and supply chains.

An interviewee from a multinational food and drinks company explained:

> The sanctions [for non-compliance] should be smart enough… and building and enabling environments to really incentivise companies to do the work properly and seriously. So meaning not being afraid of disclosing anything.
>
> If you [look] again into the UN Guiding Principles, there is the clear statement that having a proper and serious human rights due diligence process in place should help companies themselves in case they are trapped in a dispute. So in some way conducting [due diligence], if it becomes mandatory, should help companies to know and show their issues and to be safe of disclosing them. If it's again a way to blame and shame it will not be a good legislation.

However, interviewees explained that a due diligence defence would not enable a company to hide behind having had no knowledge of the specific impact or risk. An interviewee from an international civil society organisation explained:

> I would be looking at why were they not aware. That could be a failure in itself. Can they possibly justify that they were not aware of that's what they do, that's their business, that's their market, what they're there for? Why were they not aware? … It may go to the concept of 'due' … but one of the things that we find is that companies are not prepared to put [in] the money that is necessary to become aware. So in that "reasonableness", there is a lot of subjectivity in terms of: 'Ok, it is not reasonable to ask me to spend 10 million dollars to find out what the risks are', but from our perspective a big company, or even a small company that wants to work in an inherently dangerous environment, has to be prepared to put that amount of money.

It was also highlighted that in some areas of law, such as health and safety or product liability, strict liability without a defence already exists. In these cases, a due diligence defence should not apply as it would water down an existing stronger legal mechanism. An interviewee from an international civil society organisation explained:

> There are areas in which there is strict liability or objective liability already under existing law, and there is no due diligence [defence]. And many of the areas that we look at, for example mining, and other industries that work with inherently dangerous products or substances or inherently dangerous environments…the company has to respond to the damage regardless of any due diligence. And that needs to be preserved. These discussions on due diligence should not now water down existing absolute liability or strict liability…There is no due diligence [defence]. The due diligence is only to avoid the harm, but if the harm occurs the liability is automatic.

5.4.3 On application to the supply chain

Interviewees expressed opinions about how regulation requiring mandatory due diligence could be applied along the supply chain:

> When it comes to liability around supply chain issues, to be frank, there are differences in opinion as to what people want to see. Some people think: 'Well, really reasonably, can you hold someone responsible for something that happens way way down the supply chain?' I think, in theory, yes you can, because you can say, 'Well, you ought to have known what was going on'. I think the question then comes up around resourcing. If you are a really small company, where does that responsibility end? No-one is that sure of what that looks like.

Another interviewee with legal expertise on the development of the Swiss legal proposal for mandatory due diligence, emphasized the importance of ensuring that the due diligence does not simply allow companies to "force a supplier in the supply chain to sign a contract" that the supplier will itself undertake due diligence. In this regard, they indicated that it is important to base the due diligence requirement on the UNGPs, including the "three steps approach" of "identifying, taking measures and take account". This "would clarify that it is not enough to simply make the suppliers sign the contract that itself will conduct the due diligence" but that there are "different steps that needs to be taken by the company".

They added:

> [T]here is absolutely no court decision on this, so we cannot now know for sure how the first judge will decide a case about whether a company has applied its

due diligence in practice or not. We do not yet know if the judge will interpret it in restrictive way or in a broader way in accordance with the idea of the UNGPs. This is a big question that has to be addressed. This why I would recommend for legislation to be broad, but really to follow the idea of the UNGPs with regard to due diligence. This will exclude the idea that due diligence is completed when someone [in a supply chain] signs a document."

They further explained how supply chains are regulated in existing mandatory due diligence laws or proposals, as follows:

> We have to distinguish two different things. Let's start with the French law. It establishes a vigilance obligation that applies to suppliers as long as they have an established relationship with the company. The law limits the scope of liability in the supply chain based on the relationship between the supplier and the contractor: they have to have an established relationship. All others that do not have established relationship are excluded.
>
> In the Swiss constitutional initiative, we used another word: economic control. You can be liable for the damage caused by suppliers over whom you have economic control. This was precisely to include cases like the Kik case, in cases in which you have a practical economic control.
>
> These approaches in France and Switzerland both go in one direction on how to limit liability in the supply chain, based on the relationship. Because we need a limitation to some point.
>
> The other option in the German [unofficial draft outline] … That does not look at specific relationship between the supplier and buyer, but more generally at the risk. This I find is correct in the idea, but more complicated. What is a big risk? This will leave a very big margin of appreciation for a judge, which from a justice perspective would be better, but for businesses would leave too much room and uncertainty…
>
> There must be some kind of test of adequacy. This is normal, this is the case when you are applying general principles to a specific case. There will have to be a test for adequacy, but this is not enough for the specific problem in the supply chains, to say: 'Okay, when do we establish liability when don't we establish liability?'. And this is what businesses want to know. Adequacy will not resolve the problem, but the notion of a specific control or established relationship, they will say 'Okay, this is not an established relationship, I am outside of the scope of the legislation'.

Company interviewees confirmed that it was important to understand the scope of the supply chain for the purposes of extending a standard of care. It was emphasized that it would accordingly be important for any mechanism to take into account the realities of the supply chain in question.

One interviewee from an environmental NGO warned against the potential negative unintended consequences of increased supply chain due diligence for smallholders:

> One of the principles of due diligence is that in theory you're not supposed to just abandon risky suppliers, you're supposed to continue engaging with them but I don't know in practice how that works ... The cocoa sector is almost entirely smallholders. If such a regulation resulted in an increased cost for them for example, this would not be what we want, and also if it led to more small size actors being shut out of the supply chain because it's easier to conduct due

> diligence with bigger actors then this would also be something that we would be concerned by.

5.4.4 Company law and the duties of the Board

A few interviewees stressed the importance of introducing a regulatory standard within the company law framework. A survey respondent from an industry organisation indicated in an optional text box that one of the "key factors of success" for their members' due diligence has been:

> Transversality and breaking of silos: a wide variety of actors in the company must co-operate to set up and implement a plan, and then monitor and control it. Accountability for CSR should be clearly assigned and approved at the most senior level of the company.

The approach of introducing mandatory due diligence as part of the statutory duties of a company is discussed in the Regulatory Review under the heading relating to oversight and enforcement.

Beate Sjåfjell, corporate governance expert and project coordinator of the SMART Project, explained this approach with reference to the Norwegian law relating to women on Boards (which is discussed in Section 3 Regulatory Review):

> Norway took what was then seen as a very radical step and introduced rules in its public companies act, not just for listed companies but all public companies, that they have to put a minimum of 40% of women on all boards. This has really shocked my colleagues in the US and Australia, that the sanction would then be that the company would not exist anymore if this was not followed up on. This is taking it seriously as company law. If a general meeting says: Actually we do not need a board, we can manage without a board, or if they have to have an auditor, which the largest companies have to have, [and they say:] no we don't want to have an auditor, or we don't feel like submitting our annual accounts this year, then there would be very strong sanctions. And at the end of the day the company would not be allowed to exist anymore. So what they did in Norway with gender is that they took that as seriously as the rule that all boards for public companies have to have at least three members.
>
> So what we want to do is go a little bit further in that direction, and see if we take this seriously, not as some kind of CSR add-on, but see it as sustainable company law, sustainable corporate governance, what is then the best way to enforce this kind of requirement.

An important feature of the corporate law approach is that it engages the responsibilities of the Board. One company interviewee indicated that it is important to get the "involvement of the Board of directors":

> It has to go together with the annual accounts and the responsibility of the liability of Board of directors. And then everybody starts to get nervous. And I think it's positive, let's get them nervous so they will act.

Another interviewee from a multinational company stated:

> Board members have personal liability in most constructions of companies. I think that's mostly about financial data, it's not about responsible behaviour. So that could also be one of the angles to get the responsibility in the boardroom. What are the incentives used within companies? What is the incentive structure?

5.4.5 On cost

The costs and benefits analysis is set out in detail in the assessment of the regulatory options below.

However, certain comments made during interviews were particularly relevant for the consideration of stakeholders' views on the regulatory options. In particular, many interviewees within companies indicated that they would not foresee any additional costs, as they are already addressing these risks.

For example, one interviewee from a multinational company indicated:

> For us it wouldn't be an additional cost in the sense that we're already doing human rights and environmental due diligence…We have a lot to gain by making sure that everyone else is also doing this.

Moreover, interviewees indicated that a lack of undertaking due diligence is a greater financial risk to the company. Another interviewee from a multinational company indicated:

> What is costly, in my opinion, is not to do it. That is what is costly and that is what companies should understand.

The interviewee further indicated that any regulation should apply to all companies regardless of size because "it's only expensive when the responsibility falls on a limited number."

A survey respondent from a trade union association have also highlighted the importance not to take only into consideration additional costs for companies in case of regulatory actions at European level, but also to "take into consideration the costs caused to society by operations of corporations and their contractors in the supply chain which violate human rights and social rights and damage the environment". They added the importance to "take into consideration the potential improvement in companies' sustainability linked to the introduction of new rules on supply chains due diligence".

> Any analysis should therefore consider the costs and the negative impact of human rights violations in companies' supply chains in the current situation, as well as the negative environmental and social outputs.

They also underlined the importance of taking into consideration the possible benefits for society of a European initiative which would ensure that operations of corporations and their contractors in the supply chain respect human rights, social rights and the environment.

5.4.6 A "smart mix" of measures

Many stakeholders indicated that mandatory due diligence fits in with the "smart mix" of measures which is required to affect real change.

The origin of the concept of a smart mix in this context is the Commentary to UNGP 3:

> States should not assume that businesses invariably prefer, or benefit from, State inaction, and they should consider a smart mix of measures – national and international, mandatory and voluntary – to foster business respect for human rights.

Marilyn Croser, Director of CORE, who is leading the campaign for mandatory human rights and environmental due diligence in the UK, describes how mandatory due diligence fits in with the smart mix as follows:[323]

> While mHRDD and parent company liability is not the sole solution to a range of problematic corporate behaviours, it is a key part of the effort to make corporates accountable and to shift to more responsible business models.

An interviewee from an international network of NGOs which promotes corporate accountability with a particular focus on the OECD Guidelines explained that:

> In general, thinking of policy coherence, and clearer coherent messages around due diligence from governments to businesses, I think that certainly experimenting or moving towards a 'smarter mix' of voluntary and binding elements coming up from governments is going to be necessary.

For instance, in relation to deforestation, an interviewee working from an environmental NGO indicated that:

> Even if the company is trying to the best of its ability to stop deforestation, there are many drivers of deforestation that are not within its control. And in particular, what's often left out of these voluntary approaches is the role of the government in a producer country. And so, for example when there is a situation where the way that tenure rights over lands or trees are allocated is driving deforestation, so in Ghana and Côte d'Ivoire for example, the government owns the trees, not the farmers. And this ends up becoming a big incentive for deforestation ... This is an issue that companies cannot resolve, governments need to resolve that. But because so much of the conversation has focused around voluntary company commitments, we have completely lost sight of the role of producer-country governments and legal enforcement. A lot of these activities are not in line with international human rights law but they are not even in line with the law of the producer country...
>
> That's why what we're advocating for is a due diligence regulation, but also accompanied by much stronger support and processes in producer countries to improve legal enforcement. Because that brings back into the limelight a very important actor into this whole situation. And does not focus only on the supply chain, which is not going to fix a lot of the broader issues, including for example poor land use planning and uncoordinated land use planning between different ministries, which is a big driver of deforestation as well.

In relation to child labour, an interviewee who works in an international NGO indicated that:

> In the smallholder context, and if you look at child labour, child labour really is a symptom … There needs to be an acknowledgment that having impacts cannot be achieved through addressing a symptom. And I think that is where we need to define a context, so that the actors feel comfortable in taking a different approach, and not be measured by the numbers of what they report on. So [it requires] shared responsibility, coordination of actors, identifying stakeholders to engage with, helping to improve government systems and structures …That needs to be something that needs to be really spelt out so that they know that it is something that is required of them … And I think this is the challenge that we

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[323] Marilyn Croser, "Towards mandatory human rights due diligence in the UK: Developments and opportunities", *BHRRC* (3 June 2019), available at: https://www.business-humanrights.org/en/towards-mandatory-human-rights-due-diligence-in-the-uk-developments-and-opportunities.

> are currently having. It is always like: 'Oh no, this is not our responsibility, this is the duty of the government.'… But in this context, you really need to redirect your actions to help putting the required systems in place.

Another interviewee from the same organisation added:

> It is fair to try to establish some degree of responsibility on companies' side. But it would be very important almost to mandate to them to work in close cooperation with either development actors or national actors and civil society on the ground, to ensure that any effort in not happening in isolation, is not a duplication of work, or is not even in competition with what other actors are doing. And most of the time, a company is not necessarily as well placed as an international organisation to work in a way which is organic with the existing National Action Plan for instance.

One interviewee from a company which has a dedicated supply chain due diligence focus indicated that:

> On the one hand, due diligence is important to spread that awareness throughout supply chains. But it does not necessarily solve the issue that is the main problem, which sometimes requires quite some investment, engagement, market access against specific terms and a lot of external assistance … Legislation is one of the tools that can be used to do that, but you need all these different tools to be in place to actually address the issues.

The interviewee added:

> To be able to actually have a positive impact and social and environmental concerns throughout the supply chains, you need mechanisms in place. Also, maybe reward and maybe even push companies to report on the impacts you have made, and say you will actually be evaluated on whether you have actually improved environmental performance somewhere, or whether you have increased incomes somewhere…

One interviewee who works with businesses in the implementation of the UNGPs indicated the need for a package of measures, whereby the EU Member States, as home states to transnational companies, need to commit to put in place certain measures. The interviewee indicated that such measures could include making available the Member States' foreign diplomacy support and their trade missions, in order to support the expectation that business should undertake due diligence.

Several interviewees suggested that it would contribute to policy coherence if mandatory due diligence could be tied to trade incentives and conditions in trade agreements. For example, an interviewee who works with businesses in the implementation of the UNGPs indicated:

> That's a really important element to consider in any proposal that would come from the Commission level which is, we're not just saying to member States you should adapt your regulations so that they include this requirement, whether it's reporting or something that is more comprehensive due diligence expectations, but it has to have some guidance as to what kind of implementation machinery needs to sit around that. Whether it's the State also using its own economic power to set incentives for business through procurement, but also through what State-based financial institutions are required to do. Is the Development Finance Institution considering this? Is the Export Credit Agency considering this? So getting States to see that there is an array of policy measures that would be necessary to sit around any type of legislation.

And I think that that is still true when you come to the more comprehensive mandatory [due diligence] approaches like the Swiss or the French because at the end of the day, liability under those regimes will be restricted to a smaller group of entities or to impacts happening in connection with a smaller group of entities in the value chain. It's kind of impossible to imagine it otherwise under any current system of liability in those major jurisdictions. So if that is the case, how is the State going to, at the same time, send the message to business: 'But we're serious, we want you to still think about the whole value chain'. We know that you are going to expand energy on the narrow group of entities, whether it's the narrower definition in the Swiss proposal or the slightly more expansive definition in the French *devoir de vigilance* law, but it's still a subset of all the business relationships that [due diligence] is really asking companies to look at.

So I think that remains a very important question and it ties also to the European Commission' sustainable finance agenda because the expectations of investors, for example, particularly large State investors - public pension funds and so forth - is going to be one very good way to continue to send a signal to business: 'Now we're worried about the whole thing. You might be liable for this subsection, but we're looking at your performance across this whole terrain of relationships'.

Another interviewee from an international civil society organisation suggested that EU Member States' support for and encouragement of improved conditions and law enforcement in host states would be a natural complement to an EU-level mandatory due diligence law, as follows:

It needs to be a package of measures that could include also market access regulation. It needs to include definitely also measures in the producer country. There needs to be law enforcement in the producer country as well. And for that also maybe EU support to the partner countries so that they have enough resources to enforce the law in their own country… It's both an import regulation … and at the same time there is bilateral agreements, there is due diligence and so on…

If we only put due diligence regulation, the companies will say: 'Yeah, but it's not my fault, I am buying, but in that country the law is not enforcement, minimum wages are not enforced, child labour law is not enforced. It's not my job to actually enforce the law.' So I think it needs to be really combined … It is often production in very poor countries where the governments have very limited capacities … but the idea to combine a market incentive with the due diligence aspect…

I think we really need a package of complimentary measures. Just one puts pressure just really on one actor, and then it doesn't really fit together…because [producer countries] also tend to say: 'Yeah, why are you telling us what to do in our country, when your companies are coming and exploiting our people'. So if you say: 'Yeah, but they have due diligence [legal requirements in the EU], then please do something yourself', so that all the stakeholders involved have their part to play. Otherwise they keep throwing the ball at each other and saying: 'It's not my fault, it's their fault.'

One interviewee from an environmental NGO indicated that:

For us it is also important ... going beyond legality of the country of origin… Especially when we talk about deforestation, just to give you an example, in Brazil about 88 million hectares of land can still be deforested legally under the current Forest Code ... Also you need to make a differentiation, and it's also what we have experienced with companies, what's written on paper is not necessarily the reality on the ground … So you might have very good laws on the ground, but the implementation is a big failure. So for us governance is a big issue.

One interviewee who works with companies on their due diligence practices referred to the importance of schemes such as the EU Generalised Scheme of Preferences ("GSP"):

> A lot of companies we work with import into the EU under this trade scheme [the EU GSP], and it's a real driver of economic growth in certain developing countries. And it's usually valuable to European companies and consumers because they benefit from cheaper goods. I think it's important to highlight these trade schemes and the global trading system more generally, because I think greater harmonization is needed between this agenda and the agenda of the WTO or the European Commission's Trade DG. We need to be talking with one voice here, human rights due diligence is a political issue, an economic issue, it's not just human rights. We want to focus on inclusive economic growth, not just applying another layer of regulation that means the company [would] have to report … I just wanted to highlight the importance of these trade programs and the importance of trying to ensure that whatever legislation is done is interlinked with these trade programs. And [that] it's at the very least consistent with, and supportive of those trade programs' aims, which is inclusive economic growth in emerging markets economies.

In an informal interview, Professor Olga Martin-Ortega, who has worked extensively on public procurement and human rights,[324] also emphasised the importance of extending due diligence requirements to public buyers in their public procurement activities. She highlighted that this is approach is in line Guiding Principle 6 which provides that "States should promote respect for human rights by business enterprises with which they conduct commercial translations", and its Commentary which elaborates that such commercial transactions include their procurement activities, and added:

> If you incorporate the public procurement part [into a mandatory human rights due diligence legislation], what you are doing is creating an obligation on public buyers to exercise due diligence … [So] you are actually creating a larger demand for products that have undergone a human rights due diligence process and with a supply chain that has due diligence … It is the next step up in ensuring that the whole chain is covered by the due diligence requirement, it is just that the end purchaser is not the brand, the end purchaser is the public buyer. This is essential for States to comply with their own duties to protect human rights. We cannot be demanding something of companies which we are not implementing on our own purchasing processes. There is a flagrant lack of policy coherence in this regard.

In an interview, Beate Sjåfjell, corporate governance expert and project coordinator of the Sustainable Market Actors for Responsible Trade Project (SMART) funded by the EU's Horizon 2020, indicated:

> It is so exciting now that this push is coming from two different directions. So you have Action 10 of the Sustainable Finance Action Plan, which opens up for the first time...in an EU context ... for integrating sustainability into the duties of the Board. That is so important. And then from the other direction the call for mandatory due diligence for human rights. But this needs to be combined in my opinion.

[324] Olga Martin-Ortega and Claire Methven O'Brien (eds), *Public Procurement and Human Rights: Opportunities, Risks and Dilemmas for the State as Buyer* (Edward Elgar, 2019); Olga Martin-Ortega and Claire Methven O'Brien "Advancing Respect for Labour Rights Globally through Public Procurement", 5(4) *Politics and Governance* (2017), available at: https://www.cogitatiopress.com/politicsandgovernance/article/view/1073/0; United Nations Office for Project Services ("UNOPS"), "The SDGs, human rights and procurement: an urgent need for policy coherence", in *High Impact Procurement: Supporting Sustainable Development* (2017), available at: https://content.unops.org/publications/ASR/ASR-supplement-2016_EN.pdf?mtime=20171214185155.

> In the same way as the NFRD has not been able to realise its full potential because it has not engaged properly with company law and the duties of the Board; in the same way if due diligence for human rights is just placed somehow into legislation without proper consideration and reform of the description of the duties of the Board, and preferably also the purpose of the company, but definitely the duties of the Board, then we risk that it just becomes another box-ticking exercise. But if we use this opportunity so that we can also clarify the duties of the Board…
>
> But because of the dire situation that humanity is in, we need to do more than clarify that 'okay in boards you are actually allowed to do this'. We need to include in some way a mandate that they shape their business models in a way that will promote sustainability. So that we can get a race to the top, instead of to the bottom as we have now. We need to get some kind of floor in. And we need to also do that in a way that does not just focus on the single legal entity. Which is of course why this call for due diligence of human rights has come.

5.4.7 Transitional period

Several stakeholders suggested that there would need to be a transitional period for any regulation. Similarly, in its May 2018 Report on Sustainable Finance, the European Parliament, which forms the background to the mandate of this study, "[c]alls on the Commission" to provide a "legislative proposal" for "an overarching, mandatory due diligence framework including a duty of care *to be fully phased-in within a transitional period* and taking into account the proportionality principle".[325]

A survey respondent from a large cross-sectoral industry organisation explained in an optional text box:

> [M]anaging risks through global supply chains is so complex that it cannot be tackled in a snap because it involves a great number of actors at different stages. It takes several years to carry out risk analysis and put in place the appropriate procedures, which can still never guarantee a "zero risk" supply chain.

An interviewee from a civil society organisation was of the following view:

> When we think about due diligence, we need to recognise, albeit somewhat reluctantly, that companies, most of them, do not have a clue. And they are going to need really simple, ABCD, this is what you need to do. Certainly at first, I think it would take about five years before things start to move and people get an understanding of it.

Similarly, an interviewee from a civil society organisation in Poland explained that "companies in Poland are at the very beginning of understanding that their responsibility go to the supply chain". The interviewee highlighted that, although having hard law on these issues at the EU level would be "the only solution", it would be nonetheless be "a very big jump for Polish companies". The interviewee indicated:

> If we want to see any effect, the regulation should be binding. However, knowing that it won't be easy to implement it in the right way from the beginning, I do think that companies should have a bit of time to get used to it. Perhaps the regulation could be introduced in a voluntary format for the first two years, for companies to understand and train people, and already knowing that it won't be

[325] European Parliament Report on Sustainable Finance, 2018/2007(INI), at para 6.

> voluntary forever. Then on the third year, monitoring or verifying could start, and maybe penalties should apply for companies that are found not to take action accordingly. Indeed in Poland a majority of businesses are SMEs and these do need more time because they are small and do not have dedicated staff.

A number of interviewees suggested the idea of a staged approach. One interviewee who works with businesses in the implementation of the UNGPs stated:

> I could imagine that you would move from … an initial period where we make clear that this applies to everybody, including those EU member States who have not done anything on this agenda yet. We're going to give them voluntary guidance to indicate that this is real, and we're serious about it and it's coming. Then there's going to be a period when we expect better disclosure and we start to evaluate, and companies would get critical feedback from that. And that's where the connection to the investor piece becomes so important, because if you're activating investors saying: 'You have to ask companies about it, you have to look at what they're producing', then you start to get a feedback loop. And then we are going to introduce an expectation that includes the introduction of liability at national level.

The French Duty of Vigilance Law provided for a transitional period before legal action could take place.[326] An interviewee from an international trade association which works with companies on their due diligence noted, with respect to the French Duty of Vigilance Law, that legal standards need to be given content over time:

> [Y]ou might require a few test cases to set some precedence to look through them in the court, to help flash at what standards are required.

It is also noted that the France Country Report states:

> As remarked by Dominique Potier in a recent conference to mark the second anniversary of the Vigilance Law, to date we are still in a "learning phase" [*phase d'apprentissage*], where the objective is not to sanction immediately companies that are making efforts to comply with the Vigilance Law.

For this same reason, however, a transitional period may lead to a certain amount of legal uncertainty while stakeholders wait to find out how the law will be applied in practice. An interviewee mentioned that the transitional period applicable in the French Duty of Vigilance Law meant that companies have not yet had the benefit court judgments to provide clarity on how it will be applied. Guidance on the application of the French Duty of Vigilance law indicates that the first reports "are of a lightness that contrasts with the importance of the stakes of the Law on the Duty of Vigilance".[327]

5.5 Sub-options of Option 4

5.5.1 Cross-sectoral v sector-specific regulation

Survey respondents were asked about their views on the perceived potential effectiveness and impacts of different sub-options of mandatory due diligence. It should be noted, however, that these perceptions of preferences should be interpreted with caution. The regulatory options presented to stakeholders are framed within a complex and developing area of law, and there are very few existing examples to draw on. Even within the same stakeholder group (such as industry organisations) or within the same

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[326] Art 4 of the French Duty of Vigilance Law provides that legal action can take place only after the submission of the reports for the 2018 financial year (after the law came into effect in 2017).
[327] Sherpa, "Vigilance Plans Reference Guidance, First Edition", available at: https://www.asso-sherpa.org/wp-content/uploads/2019/02/Sherpa_VPRG_EN_WEB-VF-compressed.pdf, at 10.

company (depending on the respondents' department) the views may differ widely. As such, it is not likely that any single meaningful stakeholder *preference* of one regulatory option over another can be concluded in general. The following should be read bearing in mind these limitations.

Business survey respondents had a marginal preference (25.49%) for "[i]ndustry-specific regulation, tailored for your company's sector only and applying only to companies operating within this sector." This was followed very closely (24.51%, in other words only a 0.98% difference) by a preference for "[c]ross-sectoral regulation, applying to all companies regardless of size or sector."

The selection was equally close amongst business respondents with 1000 or more employees, 25.97% of which (20 respondents) preferred industry-specific regulation, and 24.68% of which (19 respondents) preferred cross-sectoral regulation applying to all companies regardless of size or sector.

Amongst medium-sized companies with 50 to 249 employees, the top preference (36.36%) was cross-sectoral regulation applying to all companies regardless of size or sector. The second choice (27.27%) was cross-sectoral regulation, applying to companies of a certain size regardless of their sector.[328] The main exceptions to the overall trend[329] were amongst micro respondents, of which 75% had no preference, and respondents with 500 to 1000 employees, where from a small sample of six respondents to this question, three (50%) preferred industry-specific regulation, and one each respectively cross-sectoral but limited by size, "both industry-specific and cross-sectoral regulation" and no preference.

Below these two choices (at 19.61% of all business respondents), the third most-preferred option by business respondents was "cross-sectoral regulation, applying to companies of a certain size regardless of their sector." These survey respondents accordingly have a preference for cross-sectoral regulation, but with limited application to companies of a certain size only.

If one adds up the responses of those business survey respondents who prefer *cross-sectoral* regulation (but disagree on application to size of company), the preference for cross-sectoral regulation outweighs the preference for sector-specific regulation: 24.51% of business respondents (cross-sectoral regardless of size) plus 19.61% (cross-sectoral applying to companies of a certain size) equals 44.12% of business respondents who prefer cross-sectoral regulation, contrasted with 25.49% which prefers industry-specific regulation.

Several business respondents who selected "[b]oth industry-specific and cross-sectoral options have their benefits",[330] commented to the effect that the standard should apply to all sectors, but should take into consideration the specifics of the sector in its implementation. For example, some of the comments from these survey respondents include:

- "Regulation would have to be tailored by industry, but it should cover all sectors."

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[328] This was followed by both industry-specific regulation and that "both industry-specific and cross-sectoral have their benefits" at 18.18% each. No medium-sized company respondents indicated that they had no preference regarding cross-sectoral regulation.
[329] Only one respondent from a small company with 10 to 49 employees responded to this question, and indicated that their preference is cross-sectoral regulation applying to all companies regardless of size or sector. There were only three respondents to this question from companies with 250 to 500 employees, and they were evenly split, with one each respectively preferring cross-sectoral regulation applying to all companies regardless of size or sector, industry-specific regulation and no preference.
[330] This option was selected by 13.73% of business respondents.

- “There is the need for a basic horizontal law covering all sectors and sizes. In addition, sector specific measures would be beneficial if paired with a smart mix of other policy measures, e.g. EU uses its trade and development policies to actively contribute to systemic issues common to the sector in question.”

- “We source cross-sectoral so it would be a benefit if all supply chains are covered. However, some industry-specific should be considered. For industry-specific, the requirements could also more specific and would therefore have a better impact.”

- “Issues are often linked to small local players, who tend to free-ride on voluntary standards”

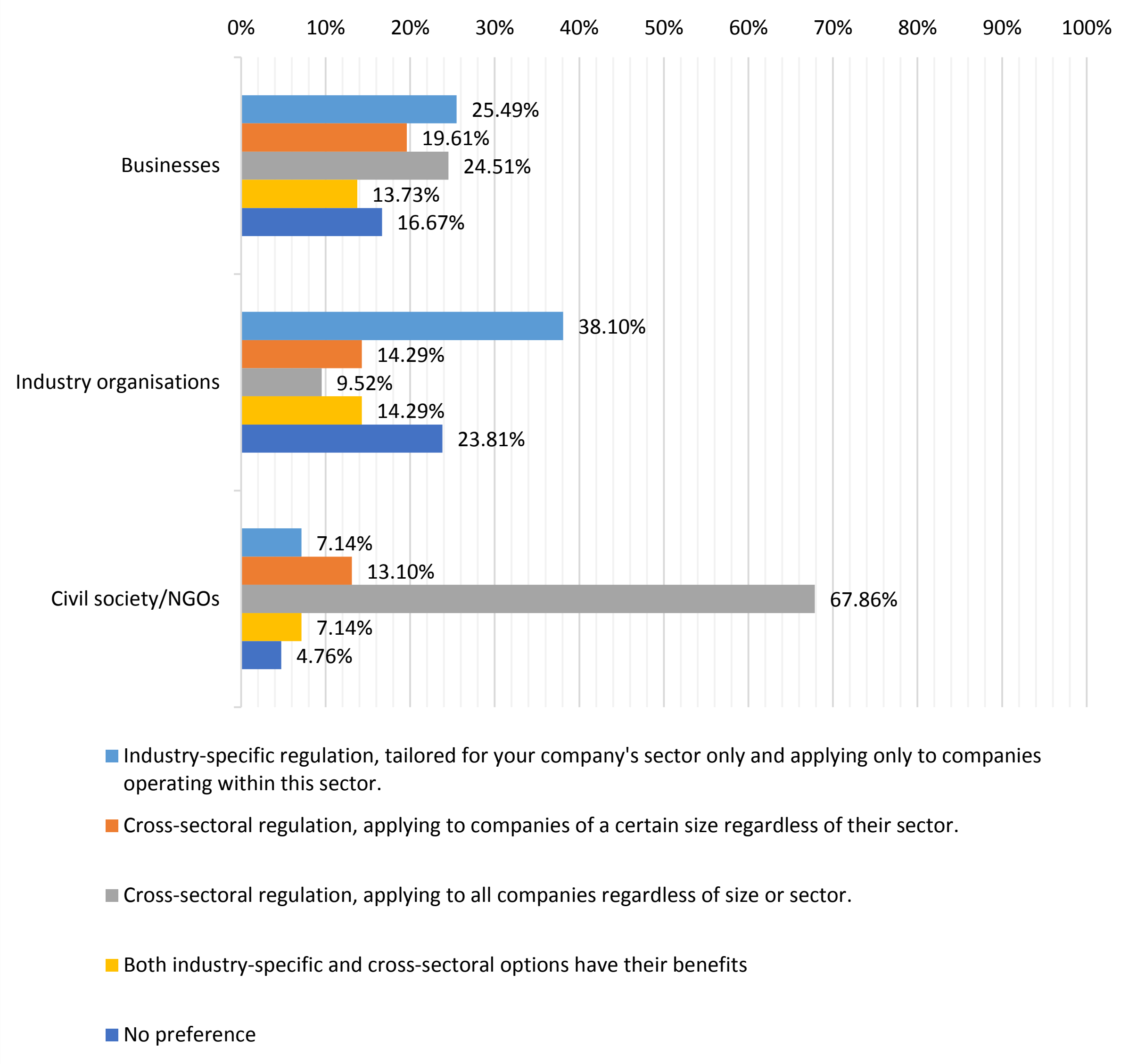
- “As many other standards such as financial reporting standards, it doesn't make sense not to treat different industries equally. It must be obvious which industry and which size of companies are responsible for violations against responsible governance.”
- “Regulations should take into account the very different structures of companies, which partly might be captured through industry specific regulations. How concentrated vs diversified is the supply chain in number, locations and types of actors. How decentralised, etc.”

General survey respondents expressed a strong preference for cross-sectoral regulation. The majority of 45.58% preferred “[c]ross-sectoral regulation, applying to all companies regardless of size or sector”. The second choice of general survey respondents (19.05%) was “[c]ross-sectoral regulation, applying to companies of a certain size regardless of their sector.”

Only 13.61% of general survey respondents selected “[i]ndustry-specific regulation, tailored for a specific sector only and applying only to companies operating within this sector.” Similarly, only 13.61% indicated that “[b]oth industry-specific and cross-sectoral options have their benefits.”

For this question, the differences between civil society and industry organisation respondents are noteworthy. Over two thirds (67.86%) of civil society respondents selected a preference for “[c]ross-sectoral regulation, applying to all companies regardless of size or sector”. In contrast, this was the least preferred option by industry organisation respondents, at only 9.52%. Instead, industry organisations expressed a preference (38.10%) for “[i]ndustry-specific regulation, tailored for a specific sector only and applying only to companies operating within this sector”, which was only selected by 7.14% of civil society respondents.

It is also informative to compare the preferences of business survey respondents with those of industry organisations. Whereas both these groups have a preference for “[i]ndustry-specific regulation, tailored for a specific sector only and applying only to companies operating within this sector”, there is a high preference for this option amongst industry organisations (38.10%). In contrast, only (25.49%) of business respondents selected this response, and followed it closely (with a margin of less than 1%) by a preference for “[c]ross-sectoral regulation, applying to all companies regardless of size or sector”, which was the least selected preference of industry organisations at only 7.14%.



Q43 Business Survey; 102 responses - Q36 Stakeholder Survey; 147 responses.

When asked to elaborate on their survey responses in optional text boxes, general stakeholders provided extensive comments, a selection of which is listed in Annexure A. Some of these comments to elaborate on their preference include:

- "As expressed in the UNGP, the responsibility to respect human rights should apply fully and equally to all business enterprises, regardless of size, sector, operational context, ownership and structure. Measures to address violations should be based on severity of impacts, scale, scope and irremediable character rather than sector or company size. If the risks outweigh the profit - which they may - then inappropriate companies will stop operating, which should be a desirable goal."

- "...A cross-sectoral regulation applying to all companies regardless of size and sector would be beneficial in a sense that it does not punish big companies over small companies. As sectors have different impacts according to economic cycles, think of commodity cycles booms and busts, it would be a way to capture all economic activity. Additional, accompanying industry specific sub-guidance or requirements could be beneficial as it can detail what a company must look at and not give too much way of interpretation of broad guidelines." [Further elaboration provided in Annexure A]

- "If a cross-sectoral regulation is pursued, it is important to provide non-binding guidelines for specific industries or types of risk, to make clearer to companies what is expected of them."

- "Whether or not a company should do due diligence, does not depend on the size of the company nor on the sector it operates in, but on the risks of possible negative impact of the company in all of its business operations and business relations."

- "EU needs human rights due diligence regulation that includes all sectors and companies. Of course regulation needs to take account that higher risks need stricter regulation and vice versa but this should not be done through artificial size or sector limits. For example company size limits implemented through employee number can create perverse incentives for companies. We also know that some of the mid-size companies operate in high risk sectors."

- "This should become a natural feature of operating a business in the EU. While industry-specific and size-specific regulation will naturally develop, it is important to have the same expectation for all."

- "There is a need for a broad and coherent framework - this does not prevent the development of specific guidelines for some sectors that are particularly at risk."

- "It is necessary to ensure that European companies – regardless of the sector they are active in – are obliged to introduce effective, comparable and comprehensive due diligence processes for their supply chains. This is necessary to ensure that the new legislation establishes a level playing field and ensures more sustainable companies' activities. The necessity to ensure that companies manage their supply chains in a sustainable and responsible way cannot be limited to a specific sector of the economy. At the same time, the size of a company is not necessarily a useful indicator to assess the dimension of the risks of human rights violations or of negative social and environmental impacts in its supply chain. For these reasons, any limitation to the necessary European legislative initiative – sectorial or based on companies' size – would not be justified and would significantly limit the positive impacts of the initiative."

- "I work on all commodities, and beyond agriculture. A relevant directive cannot be that specific - if we want "responsible coffee", we need to look at the chemicals used in the coffee plantations, we need to look at the automotive and shipbuilding industry that allows international trade, we need to look at energy. A directive can only be overarching, since our economy does not function in silos."[331]

It is noted in the Problem Analysis and Regulatory Options section that the approach whereby the same standard applies across sectors, but its content is informed with reference to the specificities of the sector, is consistent with the understanding of "due" diligence as a standard of care which would, by its nature, take into consideration the relevant operating context, including sector.[332]

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[331] This comment was included in response to the question about the agricultural subsector in which the respondent works.
[332] UNGP 14 provides: "The responsibility of business enterprises to respect human rights applies to all enterprises regardless of their size, sector, operational context, ownership and structure. Nevertheless, the scale and complexity of the means through which enterprises meet that responsibility may vary according to these factors and with the severity of the enterprise's adverse human rights impacts."

One legal expert interviewee explained how this approach would be applied in terms of a legal test for due diligence as a standard of care. They indicated that if a general cross-sectoral due diligence requirement is "applied correctly by a judge", they would expect sectoral guidance to provide content to the whether the due diligence expectation was met by the specific business in the circumstances:

> In practice there are specificities on the extent of this due diligence [requirement] for specific business in specific sectors. This is where the guidance should actually come into practice.

In this way, companies which adhere to industry standards would be more likely to show that they had undertaken the requisite due diligence even if adverse impacts should take place. In turn, the expert continued to explain why, in their view, the sectoral approach is problematic:

> "What definitely should not be pushed for is only taking a few sectors as identified on risks and to say only the business in these sectors have a human rights due diligence obligation, and not the others. This is what should be excluded...
>
> Applying a sectoral approach to say "This is a [high] risk [sector]" and "This is not a [high] risk [sector]" will definitely come with discrimination between industries, between companies. So this is why I would not recommend to go for a sectoral approach."

An interviewee from a transnational company indicated:

> There is the need for a quite a broad horizontal piece making a requirement for all businesses, that should just be part of the cost of doing business in the European Union, and everyone does want to have access to that market. But I do also see benefits potentially in doing sectoral measures.

An interviewee from civil society indicated:

> We are not in favour of a mechanism that is only applicable to certain sectors. We want a general requirement. Mainly because it is quite challenging to identify sectors that don't pose any risks. Clearly there are some sectors that pose lower risks, but it does not mean that they don't pose any. And also, the diligence is the "due" diligence. So you can make an assessment yourself as a company, "well, actually I think our risks are quite low, therefore, these are the measures that we have taken", and that's kind of the end of the matter, as it were. But given that the fragmentation is an issue, creating another range of requirements for specific groups of companies, that's quite problematic.

The fact that many companies operate across several sectors was also listed as a reason why it would be problematic to have a sectoral approach by several interviewees. An interviewee who works with companies on their due diligence indicated:

> [I]n terms of legislation, I'm not quite sure why you would pick one sector and not others. To be honest, [due to] the nature of the global economy, they're too intimate anyway. If you look at the apparel and textile sector there are lot of problems further down the supply chain. You go right down to cotton fields and that's an agricultural supply chain, that feeds into apparel and textile supply chain, that feeds in to prep general manufacturing. I think that's too interlinked. I'm not quite sure how you [could] have a different set of rules. You could have of course, guidance for different sectors stemming from legal requirements, but I don't think it would be valuable to focus on just one sector.

> Rather, I'd like to demand [the same due diligence from] major companies across the board, because we know from the UN ILO figures vulnerable work in international supply chain is on the rise, particularly in emerging market economy. It's not just one sector, and this is a problem. It is the nature of the global economy. It's where the way the business model follows the structures…That is not specific or unique to any one sector or supply chain.

An interviewee working within the government of a large Member state indicated:

> When it comes to the idea of human rights protection, it's weird to say that human rights count for some sectors and not for others. It would be incoherent for companies working cross-sectorally.

A number of interviewees suggested that a way to reconcile the need for a cross-sectoral due diligence, compliant with the UNGPs, and the need to take into consideration the specificities of the due diligence requirements in different sectors would be to adopt an overarching approach with general cross-sectoral mandatory due diligence regulation accompanied by sector-specific guidance specifying what due diligence is in the particular sectoral context. One interviewee from a civil organisation indicated in this regard:

> You would have a general framework for all sectors but then, within each sector, specific guidance. It is what the OECD does with sector specific guidance under the rubric of guidelines or guidance. I think that is something which a judge would take into consideration in a court case: what is reasonable in the textile sector as versus what's reasonable in the mining one.

An interviewee from an international network of NGOs which promotes corporate accountability with a particular focus on the OECD Guidelines indicated:

> You would want to have a general requirement because that's where the level playing field argument is coming from. And it makes normative sense because you're already expecting all companies to do it. Why single out certain ones? But then you could focus guidance or additional specifications or requirements on specific high risk sectors.

It is noted that on the question of cross-sectoral application, there seems to be some trends based on stakeholder group. There is a suggestion that large companies or multinationals in particular have a preference for a cross-sectoral standard which would level the playing field, but which is applied in a way that takes into account the sectoral particularities. In contrast, industry organisations, which represent a broader range of business than only multinationals, take the opposite view and have a preference for regulation which is industry-specific. A few low percentage of industry organisations are in favour of cross-sectoral regulation which applies to all companies regardless of size, which was the first choice for civil society stakeholders.

5.5.1 Cross-issue versus issue-specific

Survey respondents were asked about their preferences for regulation which covers all human rights and environmental impacts or only specific issues, such as modern slavery or child labour. The majority (47.06%) of business respondents preferred regulation to apply across all issues. Less than half of this number (23.53%) preferred regulation which focuses only on one issue such as modern slavery or child labour. Only 4.9% (the least selected option, below no preference), preferred "[i]ssue-specific regulation covering another specific human rights or environmental issue".

Overall, the same preferences were expressed by respondents within company size groups. 45.45% of large companies (1000+ employees)[333] and 55.56% of respondents with 250 to 500 employees preferred regulation which covers all human rights and environmental impacts. The vast majority (72.73%) of medium-sized had a preference for regulation which covers "all EU-recognised human rights and environmental impacts".[334] The main exceptions were micro respondents, of which 75% had no preference, and respondents with 500 to 1000 employees, who were evenly split (33.33% each) between cross-issue regulation, issue-specific regulation, and no preference.

Comments provided by business respondents on this question in optional text boxes within the survey include:

- "I would rather go for a regulation encompassing all EU-recognised human rights and environmental impacts, so that companies really develop a holistic framework rather than focusing on an issue and forget everything else."

- "Issue-specific regulations make life complex and costs more to companies to implement - having to have multiple processes and reporting requirements. Companies have adverse impacts on virtually all human rights, as per the UNGP foundational principle. So, from both risk perspective and effectiveness (cost) perspective, it has to be all human rights expressed at a minimum in the International Bill of Human Rights."

- "Child labour and modern slavery are two important topics, but other topics such as discrimination, harassment, working hours, etc are all important to ensure the workers are working in a good condition. In addition, it is not very practical to conduct supply chain due diligence on only one or two topics. If we pay a visit to our suppliers, we might as well cover as much topics as possible, to get the best value out of the trip."

- "Certain issues may require more in-depth disclosure such as modern slavery or child labour. However the UNGP suggested that a company should build up a management system to detect and address a broader set of human rights risks. If a regulation on mandatory HRDD then it would be beneficial to follow the guidance of the UNGP to a larger extent. This is in any case the standard that larger companies are held against. In the UNGP there are also provisions for smaller company implementation that could be beneficial to look into for the formulation should it apply to all companies."

- "Not separating out issues but rather focusing on regulating processes are more relevant.

- "It should cover all human rights."

Similarly, general respondents expressed a very strong preference (74.15%) for "[r]egulation which covers all EU-recognised human rights and environmental impacts." Only 9.52% expressed a preference for issue-specific regulation "for example covering only issues of child labour or modern slavery". The least selected option by only 2.04% of general survey respondents was "[i]ssue-specific regulation covering another specific human rights or environmental issue".

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[333] Followed by 23.38% which prefer issue-specific regulation, such as covering child labour or modern slavery, 18.18% had no preference, 6.49% preferred issue-specific regulation which cover other issues, and 6.49% indicated that both issue-specific and broader options have their benefits.
[334] This was followed by two medium-sized company respondents having a preference for issue-specific regulation, and one medium-sized respondent selecting that "Both issue-specific and broader human rights and environmental options have their benefits". No medium-sized respondents indicated that they had no preference regarding cross-issue regulation.

It is interesting to compare the responses received from civil society, industry organisation and business respondents. Both business respondents (47.06%) and civil society respondents (89.29%) had a marked preference for cross-issue regulation which applies to all EU-recognised human rights and environmental impacts. This was the third preference of industry organisation respondents (28.81%).

In contrast, industry organisations preferred (38.10%) "[i]ssue-specific regulation, for example covering only issues of child labour or modern slavery", which was selected by only 23.53% of business respondents as their second preference, and by a mere 2.38% of civil society organisations as their third preference.

One interviewee indicated that issue-specific regulation "risks that it focuses just on modern slavery, which makes sense on being an easier political entry point ... but we do see companies saying 'I've done modern slavery so I've done business and human rights'."

Similarly, one interviewee representing a trade union association indicated:

> Forced labour receives high levels of attention, but we deplore that other fundamental aspects of human rights receive less attention and tend to be less often covered in law.

Another interviewee indicated:

> "It's one of the unintended consequences [of the UK MSA] that you see: most companies have some exposure on modern slavery, but for plenty it's not their most salient issues. But a law that focuses on that is what gets the attention of their boards, and that's what drives resources and prioritization. And it's not necessarily what the UNGPs would hope that the companies are prioritizing, and it can distract from more salient and more significant issues".

The question of cross-issue regulation seems to be one aspects on which the vast majority stakeholders across the spectrum agree.

5.5.2 All companies regardless of size

As is evidenced in the Regulatory Review, some of the existing due diligence-related laws apply to certain large companies only, such as the French Duty of Vigilance Law and the EU Non-Financial Reporting Directive. Nevertheless, the UNGPs indicate that all companies should exercise due diligence, regardless of size:[335]

> The means through which a business enterprise meets its responsibility to respect human rights will be proportional to, among other factors, its size. Small and medium-sized enterprises may have less capacity as well as more informal processes and management structures than larger companies, so their respective policies and processes will take on different forms. But some small and medium-sized enterprises can have severe human rights impacts, which will require corresponding measures regardless of their size. Severity of impacts will be judged by their scale, scope and irremediable character…[T]he responsibility to respect human rights applies fully and equally to all business enterprises.

One interviewee who works with companies on their due diligence practices agreed with this approach as follows:

[335] Commentary to UNGP 14.

> I'm a proponent of the UN Guiding Principles on Business and Human Rights. The size of the company dictates what leverage they'll have … and [more is] required of and demanded of larger companies. I'd encourage you to look at ensuring consistency with the UNGPs on that level and tailoring the expectations demand, so the SMEs can comply.

As indicated above, survey respondents were asked about their preferences with respect to the different sub-options. Amongst both business and general stakeholder respondents there was a preference for regulation which applies regardless of company size.

However, varying views were expressed in the optional text boxes for the business survey about whether regulation should apply to all companies regardless of size. Some of those business respondents who were in favour of regulation applying to companies of all sizes indicated:

- "Human rights abuse and pollution could happen regardless of the size or sector. In some cases, the smaller the company, the more informal it is, and the higher likelihood of abuse."

- "[A]ll companies regardless their size or sector should be concerned by the new regulation in order to avoid free riders, i.e. small enough B2B companies which are never looked at because they are unknown to the public/consumers and can continue to operate as they wish without being under scrutiny."

- "Companies's value chain cut across multiple sectors. For effective implementation and level-playing field, it has to be cross-sectoral, and also regardless of size, because vulnerable groups are pushed into smaller and medium size sub-contractors, and we need to be able to cover them."

- "Regulation would be best if applied to all sectors and not only to big companies. Even small companies might have severe human rights risks and they often supply to bigger companies. The focus should be on knowing ones risks and working towards minimizing them which would be scalable for bigger and smaller companies."

- "We believe that in order for due diligence through the supply chains to be effective we need to get as wide participation of companies of different sizes and different industries as possible in conducting due diligence. Implementation schedules, incentives and other support measures could be considered to prioritise action. There could be differences in the level of requirements set for different sized companies and for mid-sized or smaller companies there needs to be support mechanisms and tailoring of expectations to their size. Cross sectoral regulation and other voluntary collaborative measures could be considered in order to create a smart mix of measures to drive wide-reaching impacts. Also different business sectors may benefit from each other if/when operating in similar geographical areas."

- "To reach a level-playing-field it is important, from my point of view, to require due diligence from all companies. However, at the same time, it is absolutely necessary to differentiate between companies (potential) impacts. Good indication for this are laid out in the UNGP. Though the same elements should be undertaken, the scope and depth of these need to be flexible both to relate to sector specific elements and company specific characteristics."

Other business survey respondents disagreed, commenting that SMEs should be excluded from the regulation. For example:

- “Adjusted to specific necessities within the sector but also, very important, applying to companies of a certain size.”
- “Only large companies will have enough resources to implement the mandatory due diligence. If you try to apply it to all companies, it will probably undermine the effectiveness of the regulation.”
- “Only large companies in susceptible industries should be subject to new requirements. the smaller the company, the the less regulations can be applied without harm the less international the industries supply chain, the less regulations are needed No SME should be subject to new regulations.”
- “Minimum company size should be the first criterion to be established for new mandatory regulation, as under a certain size such regulation would represent an excessive burden for companies to comply…”

Most interviewees were slightly clearer about a preference to include SMEs in the scope of the regulation. An interviewee with legal expertise relating to the Swiss counter-proposal explained the approach as follows:

> The spirit of UNGPs is based on the risk approach: your due diligence will be yours. It is higher if you work in risky sector, with a risky product or risky suppliers. It’s a risk approach. The UNGPs do not exclude SMEs for this exact reason, in that SMEs can have these risks. This is entirely correct and an approach that should be followed.

However, the interviewee added that, although the original Swiss initiative included SMEs within its scope, for “pragmatic” and “political” reasons, politicians do not want to “impose some bureaucratic burden on small enterprises”:

> The proposal which is discussed now, introduces a due diligence obligation only for big companies, and exclude due diligence obligations for small companies unless they work in risky sector. Now the problem is (and I don’t really have a solution, as this is more a political problem than a legal one), is how to find a solution in accordance with the UNGPs, which would not exclude any kind of small enterprises. The problem is that now it is for the government to decide which are the risky sectors. This is where we would come with the problems of a sectoral approach to business and human rights.

An interviewee from an international network of NGOs which promotes corporate accountability with a particular focus on the OECD Guidelines explained that the OECD Guidelines apply to all companies and "explicitly say that they represent good practices for *all* businesses". The interviewee suggested that an EU-level regulation on mandatory due diligence would ideally have "a broad application" and apply to all companies, including SMEs, but would "focus implementation or enforcement efforts on a risk analysis based on severity of risks".

Alternatively, an interviewee from Ecoda, the European Confederation of Directors Institutes, had a preference for any mandatory regulation to “start with” large listed companies:

> Start with the large listed companies because they have a much bigger impact in every sense: usually labour force, activity, turnover, suppliers, customers, number of sites, number of activities, pollution impact, corruption impact. They

> have a huge impact so they should be targeted first, because then they show the way to their suppliers, to their consumers, and to their competitors. SMEs have limited resources and specifically when it comes to their boards.

One interviewee working for a civil society organisation suggested that SMEs may be gradually included through transitional period:

> Things can go wrong at the small and medium company level … I would be reluctant to remove this group, but maybe a transitory period could be an idea to think about.

One interviewee indicated:

> As somebody who works in a [small] company … I can see how that is potentially problematic, at least at first look. When you think that I now have to do due diligence on everything that I am buying, well how on earth am I supposed to do that? I think for the majority of SMEs, I am not saying that they should not be required to do it, but careful thought would be needed about what it is they are then required to do. But I would not blanket rule small companies, because there are obviously some SMEs are that operating in what would typically be classified as high risks sectors. It falls back to that first question: therefore do you try and identify which sectors are high risk? Well, we know that's really difficult. Ultimately the only answer is that it should apply to everybody, with an emphasis on you do the due diligence that is appropriate to your size and your risk, and also obviously your leverage. Do I as a tiny company have really any leverage? Well, frankly, no. If I am a tiny company, and I am running a mine and I've decided to buy up a load of land and open up a mine there, then yeah absolutely, I do have leverage. Do I have leverage over Microsoft that I buy IT services from? No.

One interviewee working for a commerce association in a Member State where mandatory due diligence is currently being considered indicated:

> The biggest companies are on the radar of the media regarding human rights, they obviously do it for their image. But there are companies that do not have the resource or knowledge to do it, or do not find it equally important. There is a need to require it from all.

Some companies have argued that their due diligence costs would be reduced if the regulation applied to all companies, regardless of size, including SMEs. This argument was summarized as follows by one company interviewee:

> The best that can happen is that there is a law that applies not only to big companies. I mean I can understand why, I can understand the scope of legislations. But if you have SMEs understanding the Guiding Principles … Because SMEs are my suppliers. So instead of having to go to my SME supplier, and doing the due diligence in his house, if he were also obliged to apply the law or understood that it was his responsibility, then we could work together. And we'll always have my resources, I can always help you. I do always have to hold up to my standards, because I am the one with more public scrutiny that you, because you are an SMEs. But the problem with the Guiding Principles and the due diligence is that because the focus has been put only on multinational companies we have had no other way of approaching this than with a very patronising manner. So I go to an SME, which he is also a business person, he also has workers, he also has impacts, and the only thing that he does is he sits back in his chair, and he allows me to do a due diligence in his place. To understand if he has got everything okay, the contracts are okay, the workers are happy, the

community is happy, if environmentally he is not damaging the community. So let's get these SMEs involved, this will help everyone.

However, an interviewee from civil society expressed concern about this kind of approach:

> This strikes me as somewhat problematic. That kind of statement would be concerning to people who do a lot of work on supply chain issues, because one of the worries is that the powerful and wealthier actors, the better resourced actors, just shove the responsibility down the supply chain. So we have heard again of small companies being told you have to sign a declaration that says I guarantee there is no modern slavery in my own supply chain. And these small companies are saying I can't guarantee that, but I need the business, so what am I supposed to do? Now I do not think anyone has really resolved how you deal with that, it's complex and there are things that need to be consider in contract law and we have not thought that through yet. But that statement worries me that, because that does then imply that you just hold up your hands and say that we have done all that we could and it was this little guy. Now maybe in some cases that will be the situations – not everyone in the supply chains has a halo, and we all know that, but equally that would not be an effect that we would want to see.

One interviewee working within the government of a large Member State suggested a gradual approach, whereby an EU-level regulation would initially apply only to large companies, after which its scope could be broadened to the remaining companies.

An interviewee who works with businesses in the implementation of the UNGPs stated that:

> On SMEs, we've always been very skeptical of the argument that this is somehow not possible, or unreasonable to ask of SMEs. And in some ways it can be easier for SMEs to address human rights responsibilities. This is often an issue that goes to values. If you're also the owner of the business, you get to say what happens. And most owners of businesses that I know do want to be responsible employers and responsible business partners, so there's a values angle there. And there's maybe more clarity around: 'What is it that we're doing? We don't have huge numbers of diverse products or supplier lines, and we can get a handle on this'.

In a recent project working with leading SMEs, the business and human rights expert organisation Shift found that the view that SMEs lacked resources and expertise to manage human rights issues did not actually hold truth in practice.[336] In fact, they found that "small and medium sized businesses can boast significant advantages over their larger counterparts when it comes to realizing their responsibility to protect human rights".[337] In particular, they highlighted that SMEs tend to have fewer suppliers and customers, enabling deeper and better-quality relationships. Their smaller scale and inclination towards longer-term bespoke relationships can lead SMEs to engage with suppliers and their workers.[338] In addition, when top leadership of the SME is committed to respecting human rights, there are fewer obstacles to navigate than in large companies. However, Shift explained that prioritizing which issues to address is crucial for SMEs.[339]

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[336] Francis West, "SMES and the Corporate Responsibility to Respect Human Rights: Busting the Myth that Bigger is Always Better", *Shift* (May 2019), available at: https://www.shiftproject.org/resources/viewpoints/busting-myth-smes-corporate-responsibility-respect-human-rights/.
[337] Ibid.
[338] Ibid.
[339] Ibid.

This understanding of SMEs potentially having smaller footprints and accordingly less need for resource-intensive or formal processes was confirmed by an interviewee from a business membership organisation as follows:

> The difference is that in a very small company the executives and the Board, which is usually smaller and very linked to the company, are part of the game. In a big company the executives are part of the game, but at such a high level that they are far from the operations in reality. And the Board also.
>
> So I think it is right to ask those who are far from the operations to take account of all these risks and to ensure that these risks have been studied, have been looked at and documented in policies etcetera.
>
> In a small company, you could say that just need to ensure that this is looked at, full stop. Because if it is not looked at the company will die anyway, the risk is simply that high. If I am a one-man company, I look at it myself. I do it. I am the owner, the CEO and the operator.

The interviewee argued that, for this reason, the mandatory standard should first apply to large listed companies, and that more formal processes should be expected for large companies:

> As we do for financial matters. A small company can be bankrupt, and it can create many problems for its customers or its labour force at a very local level, but financially we just produce two or three documents and that's it. And you should have a similar sort of proportionality.

5.5.3 Enforcement, liability, and remedy

In order to be "mandatory", a regulatory intervention would need to establish legal liability for a failure to meet the due diligence standard. This could stake place through a state-based oversight mechanism, judicial or non-judicial remedies, or both. These sub-options for enforcement are discussed further in the Problem Analysis and Regulatory Options section.

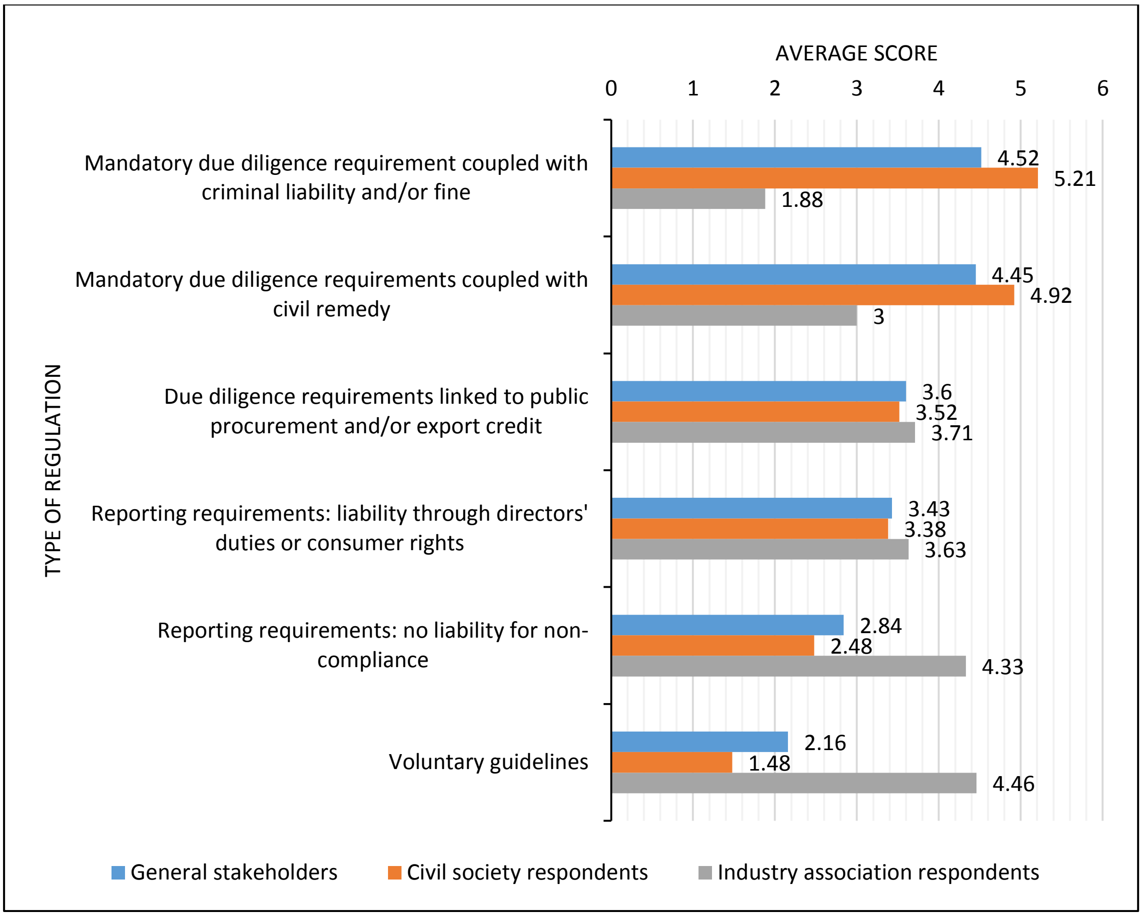
General survey respondents were asked which type of <u>current</u> regulation is the most effective.[340]

The rankings and their weighted averages were as follows, from most effective to least effective, and by stakeholder group of general stakeholders, civil society respondents, and industry association respondents.

It is notable that the industry organisation responses are in almost the exact inverse of those of civil society (and general stakeholder) respondents. In particular, civil society and general stakeholders view current mandatory due diligence coupled with criminal liability or fine as *the most effective*, whereas industry associations view these as *the least effective*. Civil society and general stakeholders' *second choice* is mandatory due diligence coupled with civil remedy, and this is the *second from the bottom* for industry respondents. Due diligence requirements linked to public procurement and / or export credit are rated as the *third most effective* by civil society and general stakeholders, and the *third least effective* currently the least effective by industry associations.

[340] This question was not asked in the business survey, which was significantly longer than the general survey, and contained more detailed questions around costs and benefits of implementation under each regulatory option.

In contrast, the type of current regulation which industry organisations view as the *most effective*, voluntary guidelines, is indicated as the *least effective* by civil society and general stakeholders. Industry associations' *second choice*, reporting requirements with no liability for compliance, as rated by civil society and general stakeholders as the *second least* effective type of current regulation.



Q14 Stakeholder Survey; 159 general responses.

The findings are interesting in that they demonstrate the directly opposing views of civil society and industry organisations regarding the effectiveness of different types of regulation.

They also reveal a bias by stakeholder group, insofar as it seems that certain stakeholders have certain preferences based on how onerous for business the requirements are, or how robust the enforcement.

For example, not only do civil society organisations rate mandatory due diligence regulation as the most effective, but those mandatory due diligence requirements with the most *robust enforcement*, namely criminal liability or fine, are rated above those coupled with less severe liability in the form of civil remedies.

It is also important to note that this question related to the effectiveness of <u>current</u> types of regulation, of which there are very few existing examples of mandatory due diligence requirements which are coupled with either criminal or civil liability (as set out in the Regulatory Review section). As such, the experiences of civil society respondents with the effectiveness of current examples of these laws would be limited, and ratings relating to effectiveness are likely to be based on preferences for future regulation (see question below). These preferences may be explained by the fact that many of the civil society organisations that participated in the survey are currently involved in campaign for mandatory due diligence developments.

On the other hand, industry organisations seem to have chosen the types of regulation which are the *least* intrusive, i.e. with the least requirements for business. Voluntary guidelines, which by their nature are not binding, were selected by industry organisations as the most effective form of current type of regulation. Although this may be a reference to the UNGPs, which is seen across the spectrum of stakeholders as the most influential standards in this area, the limitations of voluntary measures have been well-documented in the literature, as well as the interviews conducted for this study. This preference for voluntary guidelines may be explained by the following statement by an industry organisation in an optional text box:

> The risk of reputation and sanctions by the market attached to soft law is more effective than hard law and lengthy procedures. They have proven a real incentive for progress and changes.

Another interviewee from a business membership organisation explained:

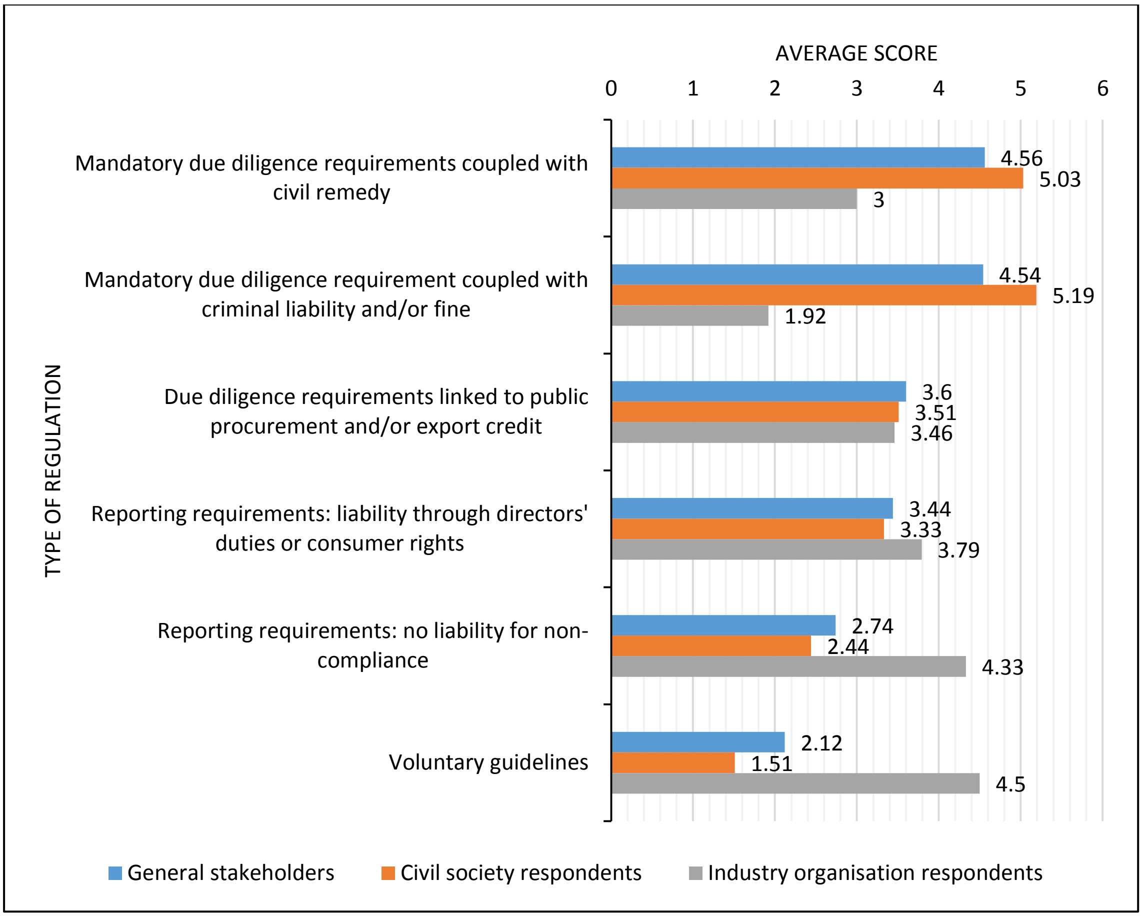
> We are of the opinion that any EU-level regulation of this matter should be confined to voluntary guidelines which should be developed in close cooperation with the companies concerned and be fully in line with already existing frameworks. The key aim of [Corporate Governance] Codes is to raise the [corporate governance] level above that required by law.

This stakeholder indicated that "mandatory regulation means this is the minimum which everybody must do" and that "you have leaders who do much better or much more than the regulation asks for and who set the trend".

However, regardless of the validity of the choice of voluntary guidelines as the most effective means of driving corporate behavior, this preference is followed by reporting requirements *with no liability for non-compliance*. Insofar as there were other reporting requirements listed which do have legal consequences or other incentives attached (through directors' duties or consumer rights), it is not clear why those currently reporting requirements with no liability attached would be more effective than reporting requirements which do lead to liability.

In all, the order in which the types of regulation were selected by both groups suggest that, rather than effectiveness, industry respondents may have selected types of regulation in order of the least to most strict or intrusive, and civil society organisations have selected types of regulation in order of most to least strict or intrusive.

In contrast to the above question, which was about current regulatory types, general survey respondents were also asked which type of regulation they think <u>should be introduced</u> for the most effective due diligence through the supply chain. The rankings and their weighted averages were as follows, from most effective to least effective:



Q15 Stakeholder Survey; 155 general responses.

Here the same observation can be made as above regarding the apparent bias according to stakeholder group for types of regulation. Again, civil society stakeholders prefer regulation from the most strict (mandatory due diligence requirements coupled with civil liability or fines) to the least strict (voluntary guidelines).

The preferences of industry organisations are in the exact reverse order. There is a preference for voluntary guidelines *to be introduced*, which is revealing, given the influence of the *existing* voluntary measures indicated by the same industry organisation stakeholders in the preceding question.

The fact that civil society and industry organisations have directly opposing preferences, and their selections follow the same order relating to both *current* types of regulation and regulation that *should be introduced*, again reinforces the impression that these selections were made not based on *effectiveness* but on *level of interference* or strictness of the regulation.

In contrast to the views of industry organisation survey respondents, which unlike other stakeholder groups seem to have a preference for regulation with no or the least amount of enforcement, interviewees from across the spectrum of stakeholders, including multinational companies, confirmed the importance of enforcement.

An interviewee from a multinational company which publicly supports mandatory due diligence regulation at EY level indicated that the mandatory character and accompanying enforcement is essential for creating a level playing field:

> It's important that it is mandatory to create a level-playing field where all the companies play by the same rules and have to incur the same costs that are associated with doing due diligence and remediation once you find the issues. So for us it is very important that it is mandatory and enforced.

A survey respondent from a trade association stated:

> Only a European legally binding directive would provide for the upwards convergence of human rights and social standards as well as environmental standards, leading to sustainable business conduct… the European legal framework should establish effective and dissuasive sanctions for any violations to companies' obligations, as well as precise liability for damages in companies' (and their subsidiaries') supply chains.

One interviewee from a multinational company indicated, regarding reporting requirements which lack enforcement:

> If there was to be a well-crafted solution at the European level, it would need more enforcement than, for example the UK Modern Slavery Act has. We're asking for a level-playing field but we also recognise that something of the nature of the UK law probably wouldn't create a level-playing field because basically it lacks enforcement.

This was confirmed by an interviewee from civil society:

> Levelling the playing field: We say that that is one of the reasons that this would be good for companies. We have heard companies, and seen it in writing, that the [UK] Modern Slavery Act, the absence of enforcement – and that is a really important point when it comes to levelling the playing field, is the need for adequate implementation and enforcement – we've seen companies saying: 'We have implemented measures in our supply chains to try to deal with issues around forced labour, and that means there is a price implication for us, and we have lost out on public contracting because our price is higher.' And they are saying that we need this to be enforced, because that's wrong.

Regarding the enforcement, the interviewee added:

> What is it that you are enforcing? Are you enforcing failure to do the due diligence? Is the enforcement around failure to do adequate due diligence, or is enforcement around the harm? And if so what does that enforcement look like?

One interviewee within the government of a large Member State indicated:

> Having a regulatory framework in place [without enforcement] does not [ensure] better protection or improvement of human rights or environment.

One interviewee from a civil society organisation indicated that:

> There is an overall duty of care demanded of international brands in terms of what they are able to do and where they are able to source it. The bar is set so low that they can knowingly source from factories that engage in exploitation. There's very little consequence in terms of legal liability. Now, their biggest problem is brand reputation - still - and media, trade union or civil society reporting on exploitative conditions. In terms of the legal framework governing international supply chain, there is very little really for them to comply with.

An interviewee from an environmental NGO stated that:

> In terms of what could be done to address the situation, I really think that ... having due diligence [should] be mandatory so that everybody has to do it, but also there being some possibility of liability is key ... The whole point is that people aren't fixing these problems, because they don't have to, basically. And if they had to, i.e. if there were consequences for not doing it, all these things that just seemed too complicated to fix, I wouldn't be surprised if suddenly some of them, not all of them, became a lot easier to fix. Because companies would actually invest significant resources and see it as a priority relating to their core business, rather than the isolated activities of a CSR or public relations department. And if they thought that they could face significant legal or financial consequences for not carrying out due diligence, including remedying or taking reasonable efforts to remedy the harms, then I think that would be a big step forward from the current situation.

The interviewee added:

> Being required to do due diligence and facing the threat of liability would make companies do much more extensive due diligence.

Enforcement through state-based oversight mechanisms

Interviewees generally indicated that a state-based oversight mechanism could be helpful in enforcing any potential regulation. One interviewee from a multinational food and drinks company indicated:

> It might also be that such a specific authority might have a better knowledge than any civil judge. And might be more understanding [of] what could be the right solution when it comes to enforcing the law. Also maybe bringing everyone around the table and look at what can be done, on top of sanctions, or in replacement of sanctions.

However, some interviewee highlighted the potential limitations or resource prohibitions of such a body.

Interviewees indicated that enforcement through state-based oversight mechanism such as administrative bodies, regulators or other government bodies would potentially be prohibitively costly.

One interviewee indicated:

> I cannot imagine that the state has the financial means to have a body that will supervise any issue about human rights or environmental impact on any company in [the country] or working from [the country]. I cannot imagine having such a big administrative authority that will be able to look at all human rights impacts in all sectors in one country. This is why I think this is a better approach to go for a civil liability, as discussed in France, in Switzerland and in other countries, also existing in the UK, to help those who were directly damaged to take their own steps before the courts.

Another interviewee from civil society indicated:

> I think there is a case to be made for criminal-level responsibility for very serious abuses. Not to diminish the seriousness of other abuses, but the political reality is the resources required. Again, we talked about this with the person working on the timber regulations. They were saying you are talking to someone who has cut a log way down the supply chain in rural Brazil. I have to get together police

> resources. They have to cooperate with the local police force, whose resources are already stretched. My resources are already stretched. Ultimately, the fine is not going to be that big. Well, really, is that going to be prioritized? And I think, frankly, in most places it isn't, and that has been the issue with the criminal approach.

One interviewee from an environmental NGO stated that:

> There needs to be actually a proper framework around the control of due diligence. I think that's something we learnt with the EU Timber Regulation: if you have no proper controls which are at least partly aligned, then you have challenges. We need to be clear in the EU: the right of implementing legislation, so checks and these things, is up to the Member States. It's their responsibility. But we do also think that there needs to be a bit more of a level-playing field amongst the different Member States and corporations. So when we talk about EU legislation on due diligence, we need to look at it from both sides: what does it mean for companies, but also what does it mean for the enforcement of legislation.

Enforcement through civil remedy

State-based oversight and enforcement mechanisms such as fines do not ordinarily provide for access to remedies for those affected by the harms. As discussed in the Problem Analysis and Regulatory Options section, victims of corporate human rights and environmental harms currently face well-documented barriers to access remedies against companies. Access to remedy is set out in Pillar III of the UNGPs and were stated by many stakeholders, especially those from civil society and trade unions, to be an essential part of a regulatory option which introduces liability. Some of these quotes are included elsewhere in this section.

One interviewee from a civil society organisation which specializes in bringing legal actions for corporate human rights abuses explained that, currently, civil liability is restricted to the existing variety of tort under civil law. Tort law causes of action are usually based on harms caused to health, life, and property interests. The interviewee indicated that this is problematic because it excludes a number of human rights that are very important.

A survey respondent from a trade union indicated that an EU-level initiative should:

> [D]efine an effective framework establishing main companies' and subsidiaries' (as well as their directors') civil and criminal liability for activities in their supply chains…
> [I]ntroduce effective and accessible remedies for victims, trade unions and other interested parties (including alert mechanisms and access to justice in the country where the main company is established), and
> [A]dequate, proportionate and dissuasive sanctions for any violation of the due diligence obligations, as well as effective monitoring and enforcement of the obligations by an independent authority – which shall be separated from the financial market authorities.

The respondent added that:

> The legislative initiative should include the possibility for trade unions to have access to effective instruments for legal recourse: trade unions' rights – such as the right to organize – are often violated and this leads to the fact that trade unions are weakened and therefore have difficulties to represent and protect workers in companies' supply chains.

5.6 Overall stakeholder views

Survey respondents were asked for their final overall views of the different regulatory options.

Although this text box was optional, it was answered by 31 business respondents. Business survey responses included the following selected comments:

- "We don't feel that further voluntary guidance or new reporting would result in desired impacts. Leading companies are applying the voluntary guidance already in existence and new reporting requirements would most likely only result in extra burden of paperwork. If the whole business sector would be active on different levels of supply networks in conducting due diligence and taking action addressing the risks identified, we believe that is where the potential for impacts lies. We also think that a support elements are necessary for smaller companies and that good due diligence should be somehow incentivised and supported. What is also important is clarity on interpretation of the meaning of the potential new requirements and quality of their implementation so that the level playing field would be created. Also the aim should be a smart mix of measures, both voluntary and regulatory with the view of creating the optimum end result."

- "We already have [Option] 2 (UNGP, OECD) and [Option] 3 (EU Directive on Non-financial reporting). These have not effected broad change. The only effective option will be [Option] 4 to create [a] level playing field. The regulation should explicitly reflect and align with UNGPs. The scope should therefore be the value chain, not limited to supply chain, and for all human rights included in the International Bill of Human Rights per UNGPs, and environmental impacts (reflecting relevant UN instruments and agreements)."

- "I would prefer mandatory due diligence, otherwise companies would find ways to report without real compliance. That is what I experience since years on the issue of sustainability and human rights."

- "To create a level playing field and mainstream the adoption of sustainable practices, mandatory due diligence is necessary."

- "We need regulations, not voluntary guidelines, to work under the same conditions and to guarantee [the] same conditions all over the world/in Europe."

- "My favourite would be mandatory due diligence in combination with mandatory reporting requirements."

- "It is recommended that human rights standards are promoted through effective trade and development agreements rather than imposing more legal requirements on business."

- "Start with step 2, guidelines. Most companies in EU are still struggling with how to do due diligence in their supply chain. Guidelines will help. Regulation should give flexibility as issues are different for different industries. Too prescriptive may focus attention away from the real issues and, in fact, not produce the required results"

- "If a mandatory due Diligence is considered: It should ONLY be considered for Human Rights and NOT for environmental aspects as they are regulated enough already."

The same question with an optional text box was completed by 90 general survey respondents, many of which were lengthy, even comprising several pages of text each. In large part, these comments are repetitive of respondent's earlier answers, already discussed above. The text box was also used to expand on questions that go beyond the selection from the four listed options.

As such, these comments are too lengthy to include here, but a selection are included in the Part IV Annexure A: Survey Responses in Optional Text Boxes. In keeping with the overall trends set out above, there is a preference amongst general stakeholders as a whole for mandatory due diligence which is a general cross-sectoral obligations, but which takes into account the specificities of the sector and other circumstances. However, a number of stakeholders, including from industry organisations, expressed a strong resistance against this option.

6. Stakeholder views on effects of EU-level regulation

Survey respondents were asked about the possible benefits of a general due diligence requirement at EU level.

6.1 Harmonisation

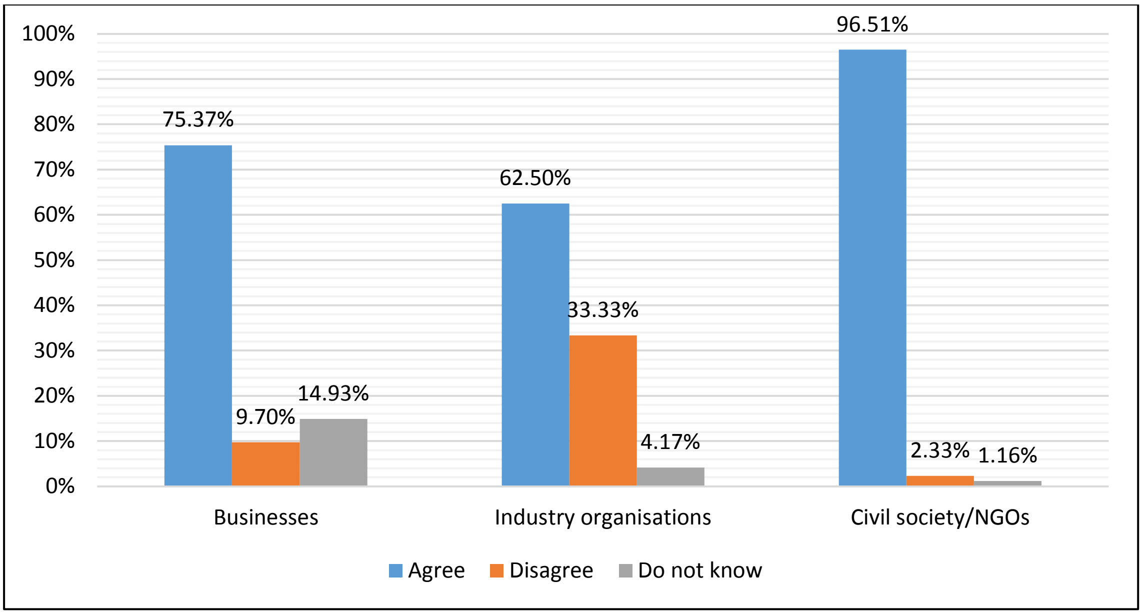
Survey respondents were asked whether they agreed with the statement that EU-level regulation on a general due diligence requirement for human rights and environmental impacts may provide benefits for business through "[p]roviding a single, harmonised EU-level standard (as opposed to a mosaic of different measures at domestic and industry level)."

The large majority of business survey respondents (75.37%) agreed that this kind of regulation would provide benefits to business through creating a single harmonized standard. Only 9.7% of business respondents disagreed with this statement about the benefits of harmonisation.

These results were slightly more pronounced among large business stakeholders with over 1000 employees: 81.25% agreed that this would provide benefits single harmonized standard, with only 6.25% disagreeing, and 12.50% expressing no opinion.

It is also revealing to contrast the responses received from civil society and industry organisations respectively to this question. Almost all (96.51%) of civil society organisations agreed that an EU regulation on a general due diligence requirement for business would benefit business by providing a single harmonized standard. Only 2.33% disagreed and 1.16% did not know. These numbers indicate that civil society respondents seem strongly convinced about the benefits which such a regulation holds for business.

In contrast, the majority of industry organisations also agreed about that such regulation would benefit business through harmonization, but in significantly lower numbers: 62.5% of industry organisations agreed about such harmonization benefits, whereas a third (33.33%) disagreed about such benefits. The remaining 4.17% of industry organisations did not know.



Q18 Business Survey; 134 general responses - Q18 Stakeholder Survey; 152 general responses.

One interviewee from a multinational company indicated:

> We find quite unhelpful that there are already quite a number of [laws or standards] and it seems many others coming at national level, which is confusing, difficult, creates complexity, uncertainty, and that is one of the reasons why we have been so outspoken about wanting a European harmonized solution.

An interviewee from a financial institution indicated:

> In general, I applaud all ideas that create an EU-wide level playing field. I do think that there is a risk now towards more fragmentation. Everybody applauds efforts in Australia to come to a Modern Slavery Act, and in the Netherlands there's been an initiative for a child labour due diligence act. But it all adds to country or sector-specific legislative requirements. So in general taking this up at the EU level also has some benefits in that sense. I would strongly oppose us having to write 5 modern slavery statements in the future just because France, Germany, Denmark, etcetera also introduced legislations.

An interviewee from an international trade association which works with companies on their due diligence indicated:

> Providing a single harmonized, legal standard at the EU level would be valuable, and from my point of view, very much desirable. It does help provide more of a level playing field in terms of what's expected at the advantage of companies within the EU. I think it also, because of the perceived…legitimacy and authority of [the] European commission and the EU institutions, I think it's more likely to be implemented and adhered to the patchwork of national legislation and different structures.

An interviewee who has been involved with the legal proposal at a national level indicated:

> What is definitely necessary is having something at the EU level to avoid that states will always have to look at what other states are doing before they start adopting their own legislation.

An interviewee from a commerce association in Finland indicated:

> It's a global issue so we do not think that it should be legislated by individual countries. The discussion should be continued at global level: UN, OECD and EU level. It is a competitive advantage to those countries and companies that do not want to comply with the rules on due diligence. So it should include as many countries as possible.

One interviewee from a multinational company indicated that the harmonization of standards will also create positive opportunities for companies:

> Most of our brand's peers and competitors are European but in different countries. It is good that we all have the same measures in this case…that we do get to speak the same language. It is also helpful because we do work a lot together, so if we get asked the same questions, it will help us standardise the way we approach things. So it will create more cohesion among brands, and that has to be dealt with at EU level. For us it definitely made a lot of sense.

6.2 Legal certainty

As set out in the Regulatory Review, companies increasingly face various legal risks, despite the lack of general legal requirement on due diligence. There are currently a number of civil and criminal proceedings in different jurisdictions against EU based companies for alleged human rights abuses in their activities or in their supply chains.[341]

Companies also face risks of legal claims under the current EU Unfair Commercial Practices Directive,[342] which may be invoked by any consumer misled.

Survey respondents were asked whether they agreed with the statement that EU-level regulation on a general due diligence requirement for human rights and environmental impacts may provide benefits for business through "[p]roviding legal certainty".

The majority (66.42%) of business survey respondents agreed that this regulation could benefit business by creating legal certainty. Only 11.94% of business respondents disagreed. Similarly, amongst large companies with over 1000 employees, 72.92% indicated that this would provide legal certainty, with only 7.29% disagreeing, and 19.79% expressing no opinion.

A contrast between the responses of civil society and industry organisations is again revealing. Whereas both groups agreed that such regulation would benefit business through providing legal certainty, 91.86% of civil society respondents expressed this view, in contrast to only half (50%) of industry organisations. Only slightly less (45.83%) of industry organisations <u>disagreed</u> that such regulation may provide benefits through legal certainty, contrasted to a mere 1.16% of civil society respondents. The remaining 6.98% of civil society and 4.17% of industry organisation respondents did not know.

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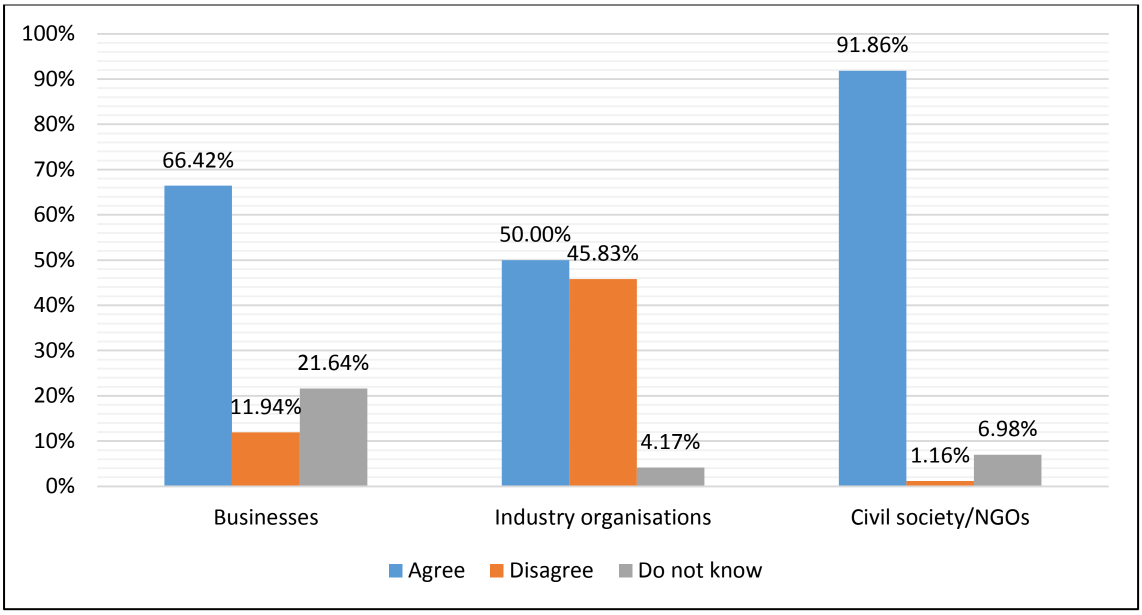
[341] Axel Marx, Claire Bright and Jan Wouters, "Access to Legal Remedies for Victims of Coporate Human Rights Abuses in Third Countries", 2019, available at: http://www.europarl.europa.eu/RegData/etudes/STUD/2019/603475/EXPO_STU(2019)603475_EN.pdf.

[342] EU Directive (2005/29/EC). This requires the company to explain how the products on the markets have been produced, not only in terms of truthful advertising but also with respect to the codes of conduct which they adopt.



Q18 Business Survey; 134 general responses - Q18 Stakeholder Survey; 152 general responses.

An interviewee from a multinational food and drinks company indicated:

> It is a problem that we have [such] different legislative frameworks, be they at early stage or already in force, because for a global company it makes it difficult to harmonise the way we establish our reporting, for example. And so far it works because we decided to have a sustainability reporting…which is quite comprehensive so that it can also be a source of inspiration for the jurisdiction where we need to make a specific report, like in the UK. But of course, having all these different approaches make it difficult to navigate because it lacks clarity [about] what is in the end expected from companies. And when companies do not know what is expected, from them by the laws, it created uncertainty, and it is not good for operating a business properly. So having a framework that would have the same criteria or the most similar criteria possible so that companies know what is expected from them would certainly be helpful.

One legal expert interviewee indicated:

> Why is it necessary to have a specific due diligence obligation in the law? Because there has been no other option in ten or fifteen years.
>
> The notion of due diligence is really being defined and redefined. It is becoming clear. It is becoming a clear notion that judges will not be able to just ignore in the future, even if it is on the level of voluntary standards.
>
> And the situation will be, we can have a common law approach, as in the UK, or in the US or in Canada, where we will have many cases coming and testing the notion of due diligence, which is not specified in the law. And this is the biggest argument, why it is desirable to have it, for legal certainty, to have this due diligence in the law.
>
> This is exactly what the European Union should do to harmonise this and increase legal certainty by introducing a clear legal definition of due diligence at the EU level.

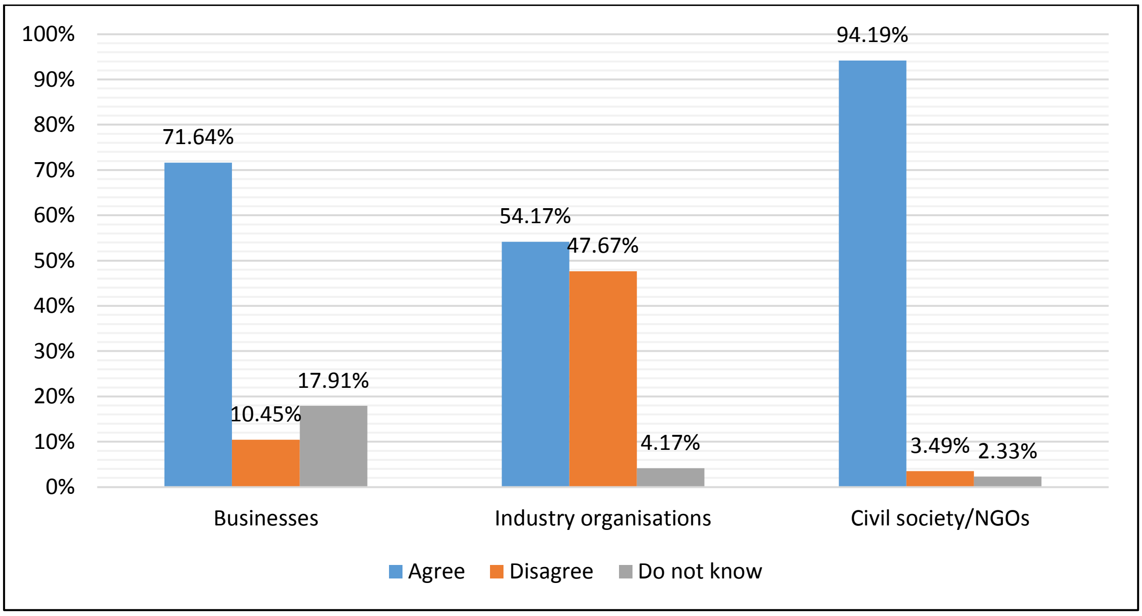
6.3 Competitiveness and "levelling the playing field"

Survey respondents were asked whether they agreed with the statement that EU-level regulation on a general due diligence requirement for human rights and environmental impacts may provide benefits for business through "[l]evelling the playing field by holding EU competitors to the same standard."

The majority of business survey respondents (71.64%) agreed with that EU regulation on mandatory due diligence may benefit to business by creating a level playing field. Only 10.45% disagreed with the statement.

Amongst large business respondents with 1000 or more employees, 73.96% agreed that this standard would level the playing field, with only 8.33% disagreeing, and 17.71% expressing no opinion.

Both civil society and industry association respondents agreed that such a regulation may provide benefits through levelling the playing field. However, civil society respondents were convinced in larger numbers (94.19%) of such benefits than industry organisations (54.17%). In contrast, only 3.49% of civil society respondents disagreed that such regulation may provide benefits through levelling the playing field, as opposed to 41.67% of industry organisations. The remaining 2.33% of civil society and 4.17% of industry association respondents did not know.



Q18 Business Survey; 134 general responses - Q18 Stakeholder Survey; 152 general responses.

Similarly, interviewees agreed that it was important to "level the playing field" by holding competitors and businesses within the value chain to the same standard. One interviewee which advises companies on their due diligence indicated that companies should "not be at a competitive disadvantage for being responsible".

One interviewee from an international trade association which works with companies on their due diligence indicated:

> I think it's a myth to say companies don't like legislation. [They] [s]ee there's red tape, [but] when it does level the playing field. Again, if they're already involved in these practices, it's all direct benefits to them. They love the companies that have the same standard and they're required to invest.

An interviewee from a multinational food and drinks company stated:

> We would be interested in a legislation that is really levelling the playing field. Because so far, you have few … companies that have already taken the journey to conduct human rights due diligence. And on the basis of that you have some free-riders that benefit from it, and in the end it might not be completely fair to put all the pressure or the weight on the biggest, because most of the time a lot of these issues happen at another level.

On 27 March 2019, Barry Callebaut, one of the "big three" companies that together process around 60% of the world's cocoa, tweeted: [343]

> An EU due diligence policy adds value by creating a level playing field among companies in driving the demand for sustainably sourced raw materials. For it to be meaningful, it has to be embedded in a strategy led by the EU agreeing action plans with origin governments.

It has been argued that considerations of creating a level playing also applies to Member States in adopting laws which require their own companies to undertake due diligence. One interviewee indicated:

> The biggest reason why countries are not adopting a law, is that they fear that they would have an economic disadvantage in comparison to others who are not taking these steps.

However, a large industry organisation survey respondent indicated in an optional text box that they are less confident about the ability of European regulation to level the playing field in the global market:

> There is still no level-playing field with many non-European companies. The gap is huge with companies from certain non-European jurisdictions, especially China and the US. Global supply chains will not improve if only European companies – already advanced with regard to CSR policies – take action.

6.4 Non-negotiable standard to facilitate leverage

Survey respondents were asked whether they agreed with the statement that EU-level regulation on a general due diligence requirement for human rights and environmental impacts may provide benefits for business through "[f]acilitating leverage with third parties by setting a non-negotiable standard".

The majority (61.19%) of business survey respondents agreed that it would be beneficial to business if a non-negotiable standard were to be created through regulation. Only 14.93% of business respondents disagreed.

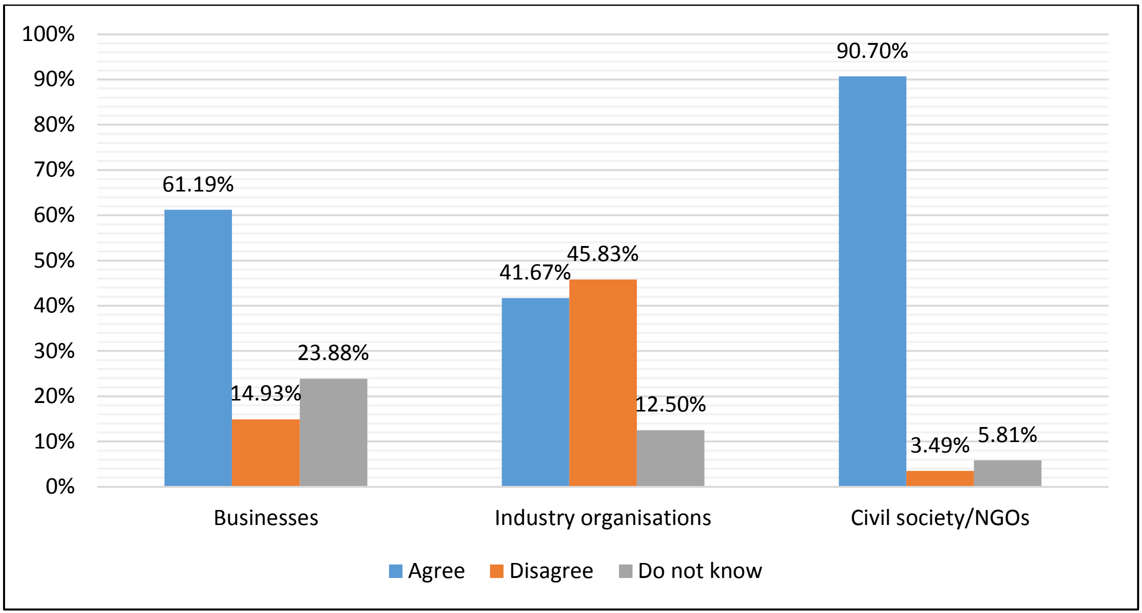
Of large business respondents with 1000 or more employees, 61.46% agreed that this could facilitate leverage with third parties through a non-negotiable standard. Only 11.46% disagreed, and 27.08% expressed no opinion.

The views of civil society respondents and industry associations were different in this respect. The vast majority of civil society respondents (90.70%) agreed that such

[343] Barry Callebaut Group: "An EU due diligence policy adds value by creating a level playing field among companies in driving the demand for sustainably sourced raw materials. For it to be meaningful, it has to be embedded in a strategy led by the EU agreeing action plans with origin governments. #MEPs4RBC", *Twitter*, 28 March 2019, available at: https://twitter.com/BCgroupnews/status/1111153494537445377.

regulation would benefit business through creating a non-negotiable standard for leverage, compared to 41.67% of industry organisation respondents. In contrast, industry organisation respondents disagreed (45.83%) that regulation would benefit business through a non-negotiable standard, a view which was shared by only 3.49% of civil society respondents. The remaining 12.5% of industry organisation and 5.81% of civil society respondents did not know.

It is notable that this is an example where the views of industry organisations are distinctly different from the views of business respondents. The majority of business respondents (61.19%) agreed about the benefits of such regulation for creating a non-negotiable standard, whereas industry associations did not agree about these benefits (45.83%).



Q18 Business Survey; 134 general responses - Q18 Stakeholder Survey; 152 general responses.

One interviewee which advises companies on their due diligence practices indicated:

> We certainly hear [companies] talking about how helpful it is in conversations with business partners to be able to point to the legislation and say: 'This is why we're asking you to do this, this is why we need you to take it seriously. It's not just because we're the good guys or we've got American values and whatever'. That can be very helpful.

However, these benefits would not always be applicable to non-EU supply chains. An interviewee from an international trade association who works with companies on their due diligence indicated:

> Most of [the] the value chains, supply chains I've been looking at, involved countries and businesses outside of the EU. It's difficult to see how a Chinese-owned company running a factory in Cambodia, for instance, that supplies several big European brands, how regulation would hold these businesses to the same standard or hold them to account. I'm not quite sure how European legislation would do that. I'm a little suspicious of that.

However, the interviewee added:

> Even though, notwithstanding what I said about the ineffectiveness about a lot of this due diligence work, some of it is down to a lack of leverage within that sector. You get a couple of brands saying the right things but many more who are saying nothing. They're not asking the right questions of their suppliers or government. [We have worked] with a couple of companies trying to do the right thing [and that] had been successful. I think it would help generate leverage within specific sectors definitely.

The interviewee further explained:

> If there [are] minimum standards in that legislation, it provides authoritative voices so companies can then go to their suppliers and say, "Well, this information is required by law." I could see the benefit of that, but I'm not quite sure. If it's information, again, for the purpose of transparency, and literal questions are being asked, yes, it would help brands.

6.5 Access to the European market

A few interviewees indicated that an EU-level regulation would be a powerful incentive insofar as it could be linked to legal requirements for operating in or accessing the European market. One interviewee from business indicated:

> It has to be tied to if you want the benefit of selling to European consumers, this is part of it.

Another interviewee from a multinational company indicated:

> We would welcome requirements in terms of what industry should do but it needs to come with the might of the EU in terms of its trade policy, of its development policy, to also be part of the solution.

An interviewee from an international civil society organisation explained how these requirements for the EU market may also indirectly lead to improved conditions in global supply chains that are not producing for the EU market:

> Many multinational companies… have EU operations and international operations. Once they do it for the EU, they will do it for the others as well. Or if they have suppliers for the EU they would buy it from the same suppliers for the others [external to the EU].

As set out in the regulatory review, some of the existing due diligence measures provide for certification of products based on human rights or environmental standards. These are frequently coupled with import restrictions of goods into the EU. One interviewee from a multinational steel company explained the shortcomings of the all-or-nothing approach of trade barriers based on certification:

> I am against certification. There are companies developing certification schemes across the supply chain, for which companies have to become members and then they certificate all your sites. Before you know it you spend a lot of money on certification. We are not in favour of that, because the rationale for such certification is if you're certified you can say 'I produce responsible steel'. But no, it will be impossible to certify, because it is not possible to consider that one has done a full due diligence and that everything is OK.

A few interviewees mentioned that import restrictions into the EU market based on the existence of human rights or environmental harms would not be feasible. One reason is because these harms are so widespread in the supply chains of all imported products.

One interviewee from a civil society organisation working on corporate practices indicated:

> When considering global supply chains, when doing research I can't remember a single case where we did not find human rights violations. The type and scope differs but there was always something.

Another reason which was stated to explain why import restrictions based on a failure to respect human rights would not be feasible was that it was not clear how customs officials would be able to check for human rights abuses in the supply chain:

> On the market access, it could be to say you cannot import into Europe products that are not produced under sustainable conditions. But of course, it's easy on environmental aspects, let's say maybe that toxic substances are not allowed, because then you can check on the product, at the customs, at the import harbour. But whether children have been involved in cocoa productions we can't check it at the harbour. So it's really difficult…

6.6 The leadership of the EU

Many stakeholders emphasized the importance of having EU leadership in this area, both within the EU as well as globally.

One transnational company based in Spain indicated, with reference to the impacts of the EU non-financial reporting directive:

> We felt that the European mandate gives some credibility … In Spain, for the last 3, 4 years, we have been struggling with changing governments. We had three elections in one month. We have one election in three weeks. So no-one really takes national laws as seriously anymore, in this moment when everything is so weird. So having Europe behind and understanding that this is a European mandate makes a big difference.

A number of interviewees referred to the beneficial spillover effects that an EU-level regulation could have for not only rights-holders, but also European companies through raising the standard globally. An interviewee working for a trade union association indicated:

> I think that it would spill over to others, for example the US. In a similar way to what we've seen with the Bangladesh Accord, which was mostly led by EU companies, and was followed by the US Alliance.

Another interview from a multinational company indicated:

> In principle, even better than EU law would be a good treaty at the international level basically turning the UNGPs into hard law. That would be the ideal level-playing field. But we have to be a bit realistic and feel that a good intermediate thing to aim for is European legislation.

An interviewee from civil society indicated:

> These things are incremental. It won't lead to an overnight change, as we know, but gradually you begin to change the dynamic. So if we put these standards in place here … At some point there will be a different administration in place in the US, so then you have a change there, you have a change in places like Canada, Australia, and things begin to shift. So obviously it's slow.

They added an important point about the EU's leadership on these issues:

> Another benefit that I could see, and would hope that this would be important to the Commission, is the European Union's commitment to human rights, and its leadership on human rights, which given the situation in the States at the minute, is more important than ever.
>
> The other one would be around the challenges that are going on to globalisation within the European Union. Obviously there are more effective standards in the EU, but there are still human rights abuses in business operations in the European Union, and if this could help European Union citizens and other people who are in the European Union, who are non-citizens, migrant workers particularly. And I think that's important. I think as the European Union tries to rediscover what it's about, that kind of leadership is crucial really. Because one of the main criticisms of [the European Union] is that it's been very good for business and it's been very good for markets, and the social aspects have been kind of left behind. And if you are going to tackle populism head-on, then these are the kinds of things that the European Union needs to be doing.

An interviewee from civil society indicated:

> In our campaign we make the comparison that, for us, it's a no-brainer that products should be safe for consumers. And we have very strong regulation on product safety. And similarly it should be a no-brainer that human rights should not be infringed on in the making of those products.

7. Conclusions: Market Practices

The following observations can be made from a study of the above market practices.

Just over a third[344] of business respondents are undertaking due diligence which takes into account all human rights and environmental impacts, and a further third[345] undertake due diligence only in certain areas.[346] Similar trends reflect amongst large companies with over 1000 employees, but survey results suggest that current due diligence practices are slightly less established within SMEs.

However, the majority[347] of business respondents who undertake due diligence indicated that third party impacts are included for first tier suppliers only. Current due diligence practices beyond the first tier and for the downstream value chain are significantly lower by comparison.[348]

The vast majority of business stakeholders expressly include environmental impacts in their due diligence, and many others view environmental impacts as implied. Although survey respondents indicated that the term "climate change due diligence" is currently rarely used as a self-standing form of due diligence, business respondents indicated that environmental impacts including aspects of climate change, air pollution and greenhouse gas emissions are viewed by business survey respondents as included, either expressly or implied, within existing due diligence processes. However, due diligence for climate change may currently often take place in other different parts or the team of the company, resulting in a "silo"-ing effect. As a result of very recent developments, there

[344] 37.14%.
[345] 33.71%.
[346] For example health and safety, labour, non-discrimination and equality, environmental, land rights and indigenous communities.
[347] 51.82%.
[348] Selected by 16.06% each.

seems to be a growing acknowledgement that climate change impacts are to be viewed within the company's own due diligence responsibilities.

The majority of business respondents indicated that income inequality is either expressly included[349] or implied in their due diligence.[350] Profit-shifting to lower tax jurisdictions is implied as included in almost three quarters of companies' due diligence,[351] and expressly included in a quarter.[352]

The terminology most frequently selected by business[353] and general stakeholder respondents[354] is "human rights due diligence". Other common terms are "sustainability due diligence" and "social, environmental and human rights due diligence". The phrase "climate change due diligence", which was the least selected phrase in both surveys,[355] suggesting that self-standing processes which focus exclusively on climate change are rare.

Stakeholders suggested that any regulatory mechanism should build upon the influence and strength of the due diligence concept of the UNGPs. The OECD Guidelines were frequently mentioned as an example of how the UNGPs concept of due diligence can be expanded and applied to other areas of responsible business conduct, as many references were made to the usefulness of the OECD sectoral guidance.

Business respondents indicated that the most frequently used actions which companies currently undertake to prevent, mitigate or remedy the adverse human rights and environmental impacts of their own operations are training on human rights or environmental impacts and contractual clauses and codes of conduct,[356] followed closely by audits.[357] Contractual clauses and codes of conduct, and audits, respectively, were also the top two actions for due diligence in the upstream and downstream supply chain.

General stakeholders also selected contractual clauses and codes of conduct,[358] followed by audits,[359] as the actions which companies take for their due diligence practice, revealing a genuine understanding of the real due diligence practices of companies among general stakeholders.

Divestment was the least selected due diligence action by both business and general respondents in both the upstream and downstream supply chain. Stakeholders made frequent reference to the concept of leverage, including the challenge of a lack of leverage. Traceability and a lack of transparency is a major challenge for companies aiming to undertake supply chain due diligence.

Stakeholders also mentioned that due diligence in this context requires the company to go beyond the risks to the company to focus on the risks to those external rights or interests affected (the "rights-holders"). Stakeholders highlighted that buying practices, including price, are a major contributor to adverse impacts in the supply chain, and that current grievance mechanisms often fall short for the purposes of identification and remediation of impacts.

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[349] 54.76%.
[350] 45.24%.
[351] 74.15%.
[352] 25.8%.
[353] 32.43%.
[354] 54.10%.
[355] Only 1.35% of business respondents and only 6.56% of general respondents use this phrase.
[356] Both at 69.01%.
[357] 67.61%.
[358] 61.76%.
[359] 60.29%.

When asked about what the primary incentives for undertaking due diligence is, or have been, business respondents and industry organisations selected the same top three incentives in the same order: Reputational risks,[360] investors requiring a high standard,[361] and consumers requiring a high standard.[362] This demonstrates that despite some divergence in views on regulatory options between these two groups (see below), industry organisations have a real understanding of the risks and incentives which drive business to undertake due diligence.

The four least selected incentives by business respondents were related to regulation or legal requirements.[363] It is notable that these are the incentives related to regulation or legal requirements. Industry organisations placed a similarly low value on the ability of regulatory measures to incentivize due diligence.[364] In contrast, general stakeholders[365] and civil society respondents[366] placed a much higher value on the role of regulation and legal risks to incentivize due diligence than business do.

Overall, the majority of stakeholders interviewed and surveyed considered existing laws on due diligence requirements for human rights and environmental impacts not to be effective, efficient and coherent. Moreover, the majority of general survey respondents[367] indicated that the current legal landscape does not provide companies with legal certainty about their human rights and environmental due diligence obligations.

Most interviewees were in principle in favour of a policy change to introduce a general standard at the EU level, although they differed on aspects of liability and methods of enforcement. However, industry organisation survey respondents were overall not in favour of the introduction of new policy changes, including mandatory due diligence.

Regarding regulatory Option 2, all interviewees across business and other stakeholders agreed that there is already enough voluntary guidance in existence. Similarly, survey respondents overall seemed unconvinced that new voluntary guidance would have notable social, environmental and human rights impacts. However, it is noted that when asked about the effectiveness of existing and possible future regulatory models, survey respondents from industry organisations had a preference for voluntary guidelines, drawing attention to the influential nature of those soft law mechanisms already in existence.

Interviewees indicated that voluntary guidance could be helpful to supplement any legal obligations. Several interviewees also highlighted that, due to the nature of due diligence, existing voluntary guidance will influence the standard of due diligence that would be expected of companies under each specific circumstance.

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[360] 66.19% for business respondents, 65.52% for industry organisations.
[361] 51.08% for business respondents, 55.17% for industry organisations.
[362] 46.76% for business respondents, 55.17% for industry organisations.
[363] Regulation which allows for sanctions or fines (33.81%), standards required for export credit or procurement contracts (25.90%), regulation which allows for judicial oversight over steps taken (21.58%) and risk of litigation by those affected (20.14%). Thereafter, the other legal-related incentives followed: risks of litigation by those affected (53.57%), regulation which allows for judicial oversight over steps taken (52.38%), regulation requiring reporting on steps taken (48.21%) and standards required for export credit or procurement contracts (45.83%).
[364] The four least selected incentives by industry organisations were regulation requiring reporting on steps taken (31.03%), risk of litigation by those affected (20.69%), regulation which allows for sanctions / fines (17.24%) and regulation which allows for judicial oversight over steps taken (10.34%).
[365] More than two thirds (67.86%) of general respondents viewed regulation which allows for sanctions or fines as the highest incentive for companies to undertake due diligence. This was followed by investors requiring a high standard (62.50%), financial risks (60.71%), reputational risks (58.33%).
[366] As many as 87.10% selected regulation which allows for sanctions or fines as the top incentive, followed by regulation which allows for judicial oversight over steps taken (69.89%), and risk of litigation by those affected (66.67%). Reputational risk was selected by only 50.54% of civil society stakeholders for incentivizing corporate due diligence, despite being the top incentive for both business and industry organisation respondents.
[367] 78.57%.

Regarding regulatory Option 3, survey respondents were more positive about the likely sustainability impacts of regulatory reporting requirements than with new voluntary guidance. However, interviews echoed the shortcomings of reporting requirements documented in the literature, particularly insofar as they do not usually provide for sanctions for non-compliance with the reporting requirement, and do not require substantive due diligence. It was nevertheless highlighted that reporting requirements have had a positive impact in raising awareness and the internal conversations within companies. It was also noted that some reporting requirements, such as the EU NFRD, are relatively new and there has not been an opportunity to fully observe their impacts on corporate due diligence activities.

Regarding regulatory Option 4, stakeholders indicated that mandatory due diligence is the regulatory options which is likely to have the most social, environmental and human rights impacts of all the options. The majority of interviewees supported the introduction of a general requirement at EU level which would require companies to undertake mandatory due diligence in their own operations and throughout their supply chains. However, interviewees differed with respect to liability and the enforcement method for implementation.

Reasons for support for such a mandatory due diligence duty at EU level, as stated by business interviewees included the levelling of the playing field, a single harmonized standard, and legal certainty. Reasons for support stated by civil society interviewees included higher levels of implementation of due diligence, prevention of human rights and environmental harms, and access to remedies for those affected. Other benefits discussed by stakeholders in relation to the introduction of a due diligence measures included facilitating leverage with third parties by setting a non-negotiable standard, access to the European market, and the leadership of the EU.

Large companies or multinationals have a preference for a cross-sectoral standard which would level the playing field, but which is applied in a way that takes into account the sectoral particularities. In contrast, industry organisations, which represent a broader range of business than only multinationals, have a preference for regulation which is industry-specific. A low percentage of industry organisations are in favour of cross-sectoral regulation which applies to all companies regardless of size, which was the first choice for civil society stakeholders.

Both business respondents and civil society respondents had a marked preference for cross-issue regulation which applies to all EU-recognised human rights and environmental impacts. In contrast, industry organisations preferred issue-specific regulation, for example covering only issues of child labour or modern slavery.

There was an overall preference for regulation which applies to all companies regardless of size amongst business and general stakeholder respondents, although some stakeholder disagreed strongly with this preference, and comments in optional text boxes emphasised concerns about the creation of a burden for SMEs. Some interviewees noted that small companies may have proportionately less risks and accordingly be expected to have less sophisticated processes than larger companies.

Relating to the perceptions of the impacts and effectiveness of mandatory due diligence, our survey suggested a direct contradiction between the views of large multinational companies and industry organisations. Survey findings and business interviews confirmed the recent trends displayed in the literature and public domain that multinational companies in particular seem to support and even call for mandatory due diligence regulation both at EU and Member State level. Reasons behind this support are stated to be the creation of a level playing field and legal certainty, two issues which particularly affect multinational companies operating across borders. Evidence of this business support is also discussed further in the Regulatory Review, where business have supported or are supports the campaigns for mandatory due diligence in certain Member States or national jurisdictions.

In contrast, the majority of industry organisation survey respondents were generally opposed to a policy change, in including mandatory due diligence regulation. As such, the views of multinational companies seemed to be more aligned with those of civil society and other general stakeholders than with industry organisations on certain key questions.

Also in relation to enforcement, the views of industry organisation survey respondents differ from other stakeholder groups insofar as industry organisation respondents seem to have a preference for regulation with no or the least amount of enforcement. On contrast, interviewees from across the remainder of stakeholders, including interviewees from multinational companies, confirmed the importance of enforcement for the purposes of effectively levelling the playing field. However, it is noted that interviewees from multinational companies did not always agree with the views of other stakeholder group interviewees regarding liability regimes and methods of enforcement.

Interviewees highlighted the importance of the use of a standard of care requirement as it would require companies to implement steps which work to prevent and mitigate human rights risks, rather than simply create processes. Many stakeholders, including all interviewees, emphasized that the standard of care should be flexible so as to take into account the specific context of each specific company, including its sector. Stakeholders across the spectrum agreed that companies should be able to escape liability if they are able to demonstrate that they have, in fact, undertaken the due diligence required in the circumstances.

A few interviewees stressed the importance of introducing a regulatory standard within the company law framework, which engages the responsibilities of the Board. Many stakeholders indicated that mandatory due diligence fits in with the "smart mix" of measures which is required to affect real change. Several stakeholders suggested that there would need to be a transitional period for any regulation.

III. REGULATORY REVIEW

1. Introduction

This section sets out the Regulatory Review carried out in accordance with Task 2 of the TOR.

2. Methodology

This section reviews the regulatory framework applicable to due diligence in the EU as well as in 12 selected Member States (including the UK) with respect to due diligence for human rights and environmental impacts in companies' own operations and through their supply chains. These particular Member States have been identified as States where there has been some regulation or other engagement by governments in the area of due diligence through the supply chain.

The country reports for this study are included in the annex Part III Country Reports. The country reports have been prepared by legal experts with expertise relating to due diligence in the relevant jurisdiction. Country experts were asked to provide their information regarding relevant and related forms of due diligence, from due diligence for specific human rights impacts and environmental impacts, to due diligence for other sustainability and governance issues. Country reports include information on legislation and other forms of regulation at national level, as well as draft legislation and regulatory proposals put forward in relevant Member States, with a particular interest in the legal models and implications of due diligence regulation. Country reports set out, where relevant, relevant industry standards, case law, and literature which provide examples of due diligence requirements for operations and supply chains. We thank our expert rapporteurs for their hard work and invaluable insights in their reports.

Before turning to the in-depth findings of the country reports, the section provides an overview of the concept of due diligence and relevant developments at international and EU level.

3. The concept of due diligence

The concept of due diligence referred to in the TOR and European Parliament report[368] which provides the mandate for this study was first introduced by the UN Guiding Principles on Business and Human Rights ("UNGPs").[369] It has since been incorporated into various other standards discussed in this study, including the OECD Guidelines ("OECD Guidelines").[370]

Different legal systems within the EU use different terminology to refer to due diligence in relation to human rights and environmental matters, which might create some confusion.[371] In particular, the common law systems often rely on the concept of duty of

[368] European Parliament Report on Sustainable Finance, (2018/2007(INI)), 4 May 2018, available at: http://www.europarl.europa.eu/doceo/document/A-8-2018-0164_EN.html, at para 6.
[369] UN Office of the High Commissioner for Human Rights ("OHCHR") "Guiding Principles on Business and Human Rights: Implementing the 'Protect, Respect and Remedy' Framework", HR/PUB/11/04, 2011 ("UNGPs"), available at: https://www.ohchr.org/documents/publications/GuidingprinciplesBusinesshr_eN.pdf.
[370] OECD Guidelines for Multinational Enterprises 2011, available at: https://www.oecd.org/corporate/mne/. See also the OECD "OECD Guidelines for Multinational Enterprises: Responsible Business Conduct Matters" ("OECD RBC Guidance"), available at: http://mneguidelines.oecd.org/MNEguidelines_RBCmatters.pdf, and the 2017 OECD Guidelines for Responsible Business Conduct for Institutional Investors, available at: https://mneguidelines.oecd.org/RBC-for-Institutional-Investors.pdf and mentioned in para 11 of the European Parliament report above n 368.
[371] Andreas Rühmkorf and Lena Walker, "Assessment of the concept of 'duty of care' in European legal systems for Amnesty International", *European Institutions Office*, September 2018.

care, which "refers to the circumstances and relationships giving rise to an obligation upon a defendant to take proper care to avoid causing some form of foreseeable harm to the claimant in all the circumstances of the case in question".[372] The term "vigilance" used in the French Duty of Vigilance law "has much more specific, codified conditions than the very general duty of care".[373]

However, the concept of human rights due diligence, which has gained a wide acceptance at the international level since the UNGPs resonates with existing standards both in civil law and common law systems, and "may be used to clarify these standards' application in the context of complex corporate structures and value chains".[374]

John Ruggie referred to due diligence as the principle of "do no harm",[375] which is a common principle in all legal systems, common law or civil, across the EU and indeed the world. In this sense, it describes the process, or rather a "bundle of interrelated processes",[376] through which businesses can identify, prevent, mitigate and account for their actual and potential adverse human rights impacts.[377]

In other areas of law, due diligence is also used as a legal standard of care. It is noted that the European Parliament report in response to the Action Plan on Sustainable Finance referred to a "mandatory due diligence framework including a *duty of care*". In this study, mandatory due diligence as a duty of care will be understood within the meaning of the legal duty or standard of care.

In this way, the term "duty of care" should be distinguished from:

- the phrase "duty of care" as it is used in the *English tort law cases* (discussed in the Regulatory Review) relating to *parent company liability* (for example, where claimants have to demonstrate that the parent company owed a duty of care to those affected by the activities of the subsidiary); and

- the phrase "duty of care" as it relates to the fiduciary or other duties which an *individual director* owes *to a company* in terms of company law.

Robert McCorquodale and Jonathan Bonnitcha have argued that the use of the term "due diligence" in the UNGPS was deliberately chosen to build a consensus, as it is a phrase familiar to business people, lawyers and States.[378] However, they argue that the meaning of due diligence as a *process to manage business risk*, [379] as it is understood in the traditional business context, differs from the meaning of due diligence as a legal *standard of care,* which is expected of a duty bearer to discharge an obligation.[380] In the UNGPs, human rights due diligence refers interchangeably to a process and a standard of care expected of companies to meet their responsibility to respect.[381]

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[372] Lexis Library, Glossary.
[373] Rühmkorf and Walker above n 371 at 5.
[374] Ibid.
[375] Ruggie summarises the corporate responsibility to respect as "put simply, to do no harm". UN Human Rights Council, "Report of the Special Representative of the Secretary-General on the issue of human rights and transnational corporations and other business enterprises: 'Protect, Respect and Remedy: a Framework for Business and Human Rights'", A/HRC/8/5 (7 April 2008), at para 24; UN Human Rights Council, "Report of the Special Representative of the Secretary-General on the issue of human rights and transnational corporations and other business enterprises: Clarifying the Concepts of 'Sphere of Influence and Complicity'", A/HRC/8/16 (15 May 2008), at para 3.
[376] UN Working Group on the issue of human rights and transnational corporations and other business enterprises, "Corporate human rights due diligence – emerging practices, challenges and ways forward", A/73/163 (16 July 2018), at para 10.
[377] UNGP 17.
[378] Jonathan Bonnitcha and Robert McCorquodale, "The Concept of 'Due Diligence' in the UN Guiding Principles on Business and Human Rights", 28 *European Journal of International Law*, 2017 899 at 900.
[379] Ibid.
[380] Ibid.
[381] Ibid.

3.1 Due diligence as a legal standard of care

The concept of due diligence as a standard of care originated from Roman law,[382] where it was used as an objective standard of expected conduct both in contract law and in the law of tort. In particular, a wrongdoer would be held liable for acts of negligence if he or she had failed to comply with the standard of conduct which would have been exercised in the circumstances by the diligent *paterfamilias* (i.e. prudent father of family/ head of the household), which would then become known in common law as the ordinary reasonable person standard.[383] Although terminologies vary, this principle that a person should exercise a certain standard of care in order not to harm another is still commonly recognized in legal systems across EU Member States.[384]

Since Roman law, due diligence has remained a context-specific concept,[385] and the standard of conduct against which fault could be assessed depended on the particular facts of the case. Roman lawyers used the example of a farmer burning stubble in his fields: If it is a quiet day and the farmer watches the fire diligently, then he could be said to meet the expected standard of conduct. However, the farmer would be liable for the damage to his neighbour's crops if he had burnt the stubble in his fields on a windy day and was unable to control the fire as a result.[386]

In international law, due diligence has played an important role in the responsibility of States for private actors.[387] It refers to an obligation of conduct rather than obligation of result which means that the primary focus is on the behaviour of the duty bearer rather than on the outcome of that behaviour.[388] The Max Planck Encyclopaedia of Public International Law defines due diligence as "an obligation of conduct on the part of a subject of law", the breach of which does not consist in "failing to achieve the desired result" but rather in "failing to take the necessary, diligent steps towards that end".[389] As such, due diligence tends to inquire whether a State has taken reasonable and appropriate steps to prevent or mitigate breaches of international law by private persons.[390]

The concept of due diligence allows for a flexible approach to performance preserving a significant measure of autonomy and flexibility for the duty bearers in discharging their obligation.[391] Further elaboration is provided on the concept of due diligence in the "Due diligence as a legal standard of care: Clarification of a few common questions" subsection of the Problem Analysis and Regulatory Options section.

3.2 Developments in due diligence

3.2.1 UN Guiding Principles on Business and Human Rights

As mentioned previously, the origin of the concept of due diligence for the purposes of this study is UNGPs. The UNGPs emerged as result of extensive stakeholder consultation

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[382] Ibid at 902.
[383] John Jefferson Bray, "Possible Guidance from Roman Law" (1968) *Adelaide Law Review* 145 at 150.
[384] See the Country Reports as well as Cees van Dam "Tort Law and Human Rights: Brothers in Arms On the Role of Tort Law in the Area of Business and Human Rights" (2011) 2 *JETL* 221 at 237.
[385] Lise Smit, Arianne Griffith, Robert McCorquodale, "When national law conflicts with international human rights standards: Recommendations for Business", *BIICL Business Network*, available at : https://www.biicl.org/projects/when-national-law-conflicts-with-international-human-rights-standards at 14.
[386] Reinhard Zimmermann, *The Law of Obligations: Roman Foundations of the Civilian Tradition*, Oxford University Press (1996) at 1007.
[387] Timo Koivurova, "Due Diligence", in Rüdiger Wolfrum (ed.), *Max Planck Encyclopaedia of Public International Law* (2010), at para 3.
[388] ILA Study Group on Due Diligence in International Law, Second Report, July 2016, at 2.
[389] Koivurova above n 387 at para 3.
[390] ILA Report above n 388 at 3.
[391] Ibid at 2.

by the Special Representative on Business and Human Rights, John Ruggie,[392] and constitute "a globally recognized and authoritative framework" for preventing and addressing adverse human rights impacts resulting from business activities".[393] The UNGPs were unanimously endorsed by the UN Human Rights Council in June 2011 and endorsed by the EU in 2011.[394] The UNGPs are organised around three pillars: the State duty to protect human rights; the corporate responsibility to respect human rights; and access to remedy for victims of business-related human rights abuses.

The UNGPs set out the corporate responsibility to respect human rights which, under Guiding Principle 13, requires business enterprises to avoid causing or contributing to adverse human rights impacts through their own activities, and address such impacts when they occur, but also to seek to prevent or mitigate adverse human rights impacts that are directly linked to their operations, products or services by their business relationships.

The UNGPs state that in order to meet their responsibility to respect human rights, business enterprises should carry out human rights due diligence ("HRDD").[395] HRDD should "identify, prevent, mitigate and account for"[396] actual or potential adverse human rights impacts a company may be involved in through its own activities or business relationships. The Commentary to Guiding Principles 17 further clarifies:

> Potential impacts should be addressed through prevention or mitigation, while actual impacts – those that have already occurred – should be a subject for remediation…

In its Interpretive Guide on the corporate responsibility to respect human rights, the UN Human Rights Office of the High Commissioner defined human rights due diligence in the context of the UNGPS as comprising:[397]

> [A]n ongoing management process that a reasonable and prudent enterprise needs to undertake, in light of its circumstances (including sector, operating context, size and similar factors) to meet its responsibility to respect human rights.

The UN Working Group on the issue of human rights and transnational corporations and other business enterprises ("the UN Working Group") notes that:[398]

> Since the endorsement of the Guiding Principles by the Human Rights Council in 2011, corporate human rights due diligence has become a norm of expected conduct.

Important concepts relating to due diligence for this study are:

- The UNGPs refer to the value chain (not the supply chain), which refers to the entire life cycle of the product or service, and includes other business partners

[392] John Ruggie, *Just Business*, Norton (2013) at 141-148.
[393] UN Working Group above n 376 at para 1. See also Shift Project, "UN Guiding Principles on Business and Human Rights", available at: https://www.shiftproject.org/resources/publications/un-guiding-principles-on-business-and-human-rights/.
[394] Responsible Business Conduct Working Group, Shadow EU Action Plan on the Implementation of the UN Guiding Principles on Business and Human Rights within the EU, March 2019, available at: https://responsiblebusinessconduct.eu/wp/wp-content/uploads/2019/03/SHADOW-EU-Action-Plan-on-Business-and-Human-Rights.pdf.
[395] UNGP 15-21.
[396] UNGP 15.
[397] OHCHR, *The Corporate Responsibility to Respect Human Rights: An Interpretive Guide,* HR/PUB/12/02 (2012), available at: https://www.ohchr.org/Documents/Publications/HR.PUB.12.2_En.pdf at 4.
[398] UN Working Group above n 376 at para 20.

than suppliers.[399] For the purposes of this study stakeholders were asked questions about both the upstream supply and the downstream value chain.

- The UNGPs expect companies to undertake HRDD for "adverse human rights impacts that the business enterprise may *cause* or *contribute to* through its own activities, or which may be *directly linked* to its operations, products or services by its business relationships".[400]

- The concept of leverage is used to determine whether the company has taken "appropriate action" in circumstances where it contributes to, may contribute to, or may be directly linked to adverse impacts. Leverage is "considered to exist where the enterprise has the ability to effect change in the wrongful practices of an entity that causes a harm".[401]

- The UNGPs are clear that HRDD should be ongoing (not once-off / pre-transactional),[402] should be context-specific (not a one-size fits all tick-box, but tailored to correspond with the size of the company, risks of severe impacts, the nature and context of operation),[403] and should cover all human rights, although certain human rights may be prioritised over others based on severity of risks.[404]

- Risks should be defined as risks to rights-holders (i.e. the people affected), and not just on the risks to the company.[405] This requires an important departure from current / traditional risk analysis processes.

The UNGPs identify four essential components of due diligence:

1) identifying and assessing actual and potential human rights impacts
2) integrating and acting upon the findings
3) tracking the effectiveness of actions taken; and
4) communicating how impacts are addressed.[406]

The UN Working group on the issue of human rights and transnational corporations and other business enterprises has also specified that the human rights due diligence processes need to be complemented by an active engagement in the remediation of adverse human rights impacts caused or contributed to by the enterprise.[407]

The influence of the UNGPs is evident in the widespread adoption and use of the concept and terminology of due diligence as the standard of care expected of companies for their human rights and environmental impacts, including in international standards such as the OECD Guidelines for Multinational Enterprises (and latest OECD Guidelines on Due Diligence for Responsible Business Conduct),[408] and in regulatory developments and

[399] UNGP 13 and its Commentary. In this study, we refer to value chain with respect to the upstream and downstream supply chain, in accordance with the TOR. However, it is noted that in certain contexts the value chain may also be understood to include further business relationships that are not part of the life-cycle of the product, such as governments which issue licenses / concessions.
[400] UNGP 17.
[401] Commentary to UNGP 19.
[402] Ibid.
[403] Commentary to UNGP 17.
[404] UNGP 17 and its Commentary.
[405] Protect, Respect and Remedy Framework above n 375 at para 6.
[406] UNGP 17.
[407] UN Working Group above n 376 at para 10.
[408] OECD Guidelines above n 370.

proposals such as the French Duty of Vigilance Law, the Swiss Responsible Business initiative and parliamentary counter-proposal for mandatory due diligence,[409] the unofficial outline setting out draft for a German mandatory due diligence law,[410] and corporate reporting standards such as the UNGPs Reporting Framework,[411] and multiple corporate reports,[412] investment benchmarks such as the Corporate Human Rights Benchmark,[413] and the work of the Office of the UN High Commission for Human Rights.[414]

The UNGPs have also been influential on policy developments in the context of the International Labour Organisation, for instance through the references to due diligence in line with the UNGPs in the 2016 Resolution concerning decent work in global supply chains,[415] and the recent revision of the ILO Tripartite declaration of principles concerning multinational enterprises and social policy (MNE Declaration),[416] as well as in the G20 (e.g. in the 2017 Leaders' Declaration on Sustainable Global Supply Chains,[417] and 2017 Declaration of Labour and Employment Ministers on fostering decent work in sustainable global supply chains) and of G7 (e.g. 2019 Labour and Employment Ministers' Communiqué and the Ministers on Commitments to Promote Responsible Business Conduct in Global Supply Chains).[418]

Andreas Rühmkorf and Lena Walker write:[419]

> [Human rights due diligence] is the term that is more common in international soft law; it has its origins in the UN Guiding Principles and is used by the OECD. It is a concept that has gained wide acceptance at the international level… [Due diligence] resonates with existing standards of duty of care in tort law and comparable concepts in civil law. It may be used to clarify these standards' application in the context of complex corporate structures and value chains.[420]

3.2.2 OECD Guidelines for Multinational Enterprises

The OECD Guidelines for Multinational Enterprises,[421] revised in 2011 to align with the UNGPs,[422] and its guidance on Responsible Business Conduct incorporate a similar standard of due diligence as that set out in the UNGPs.[423] For the purposes of our study, the OECD Guidelines are particularly relevant insofar as they extend the concept of due

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[409] See BHRinLaw "Switzerland", available at: http://www.bhrinlaw.org/key-developments/64-switzerland.
[410] Business and Human Rights Resource Centre ("BHRRC"), "German Development Ministry drafts law on mandatory human rights due diligence for German companies", available at: https://www.business-humanrights.org/en/german-development-ministry-drafts-law-on-mandatory-human-rights-due-diligence-for-german-companies. It is noted that the German Federal Government recently issued a statement stressing that the document merely constitutes "internal considerations" within the German Federal Ministry for Industrial Cooperation and Development ("BMZ"), https://www.bundestag.de/presse/hib/670510-670510.
[411] Shift and Mazars, "The UN Guiding Principles Reporting Framework", available at: https://www.ungpreporting.org/.
[412] See, for example, Unilever, *Human Rights Progress Report*, 2017, available at: https://www.unilever.com/Images/human-rights-progress-report_tcm244-513973_en.pdf; Nestlé, *United Nations Guiding Principles Reporting Framework*, 2017, available at: https://www.nestle.com/asset-library/documents/library/documents/corporate_social_responsibility/ungprf-index-of-answers-2017.pdf.
[413] Corporate Human Rights Benchmark, available at: https://www.corporatebenchmark.org/.
[414] For example, see the OHCHR "Accountability and Remedy Project: Improving accountability and access to remedy in cases of business involvement in human rights abuses", available at: https://www.ohchr.org/EN/Issues/Business/Pages/OHCHRaccountabilityandremedyproject.aspx
[415] International Labour Organisation ("ILO"), Resolution concerning decent work in global supply chains, adopted on 10 June 2016.
[416] ILO, Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy, adopted by the Governing Body of the International Labour Office at its 204th Session (Geneva, November 1977) and amended at is 279th (November 2000), 295th (March 2006) and 329th (March 2017) Sessions ("ILO MNE Declaration").
[417] G20 Leaders' Declaration: Shaping an interconnected world, Hamburg, 7/8 July 2017.
[418] Outcome of the G7 Labour & Employment Ministerial 2019, Paris 13 June 2019,
[419] Rühmkorf and Walker above n 371.
[420] Ibid.
[421] OECD Guidelines above n 408.
[422] John Ruggie and Tamaryn Nelson, "Human Rights and the OECD Guidelines for Multinational Enterprises: Normative Innovations and Implementation Challenges", *Corporate Social Responsibility Initiative* Working Paper No. 66 (May 2015), at 13.
[423] Due diligence was incorporated into the OECD Guidelines above n 370 as part of the 2011 revision.

diligence expressly to other areas of responsible business conduct, including environment and climate change, as well as risks related to conflict, labour rights, bribery and corruption, disclosure and consumer interests. For the launch of the OECD Due Diligence Guidance on Responsible Business Conduct, John Ruggie described the revised OECD Guidelines as "the first [inter-governmental instrument] to take the Guiding Principles' concept of risk-based due diligence for human rights impacts and extend it to all major areas of business ethics".[424]

The OECD due diligence responsibilities also apply to the supply chain,[425] and the OECD has produced detailed supply chain due diligence guidance for certain sectors: conflict minerals,[426] the agricultural sector,[427] the garment and footwear sector,[428] institutional investors,[429] multi-stakeholder engagement in the extractive sector,[430] and export credit agencies.[431] Stakeholders in our study (in the Market Practices section) have confirmed that the OECD guidance and the UNGPs go hand in hand for the purposes of defining and concretizing the due diligence framework on which companies rely for their policies and processes.

The OECD Guidelines also require OECD member states to set up National Contact Points ("NCPs"), to which complaints may be made that a company is in breach of the OECD Guidelines.[432] A key development in developing an understanding of climate change due diligence in practice has been the case against ING before the Dutch NCP, discussed elsewhere in this study.

It is noted that although the OECD Guidelines cover tax, this Chapter does not refer to due diligence.[433] Instead, it states that "enterprises should comply with both the letter and spirit of the tax laws and regulations of the countries in which they operate".[434] The OECD Due Diligence Guidance for Responsible Conduct further confirms that due diligence does not apply to matters of taxation.[435]

3.2.2.1 The OECD Guidelines and Climate Change Due Diligence

In light of the scope of this study, it is particularly helpful to consider the provisions of the OECD Guidelines relating to climate change. The OECD Guidelines provide that:

> [E]nterprises should, within the framework of laws, regulations and administrative practices in the countries in which they operate, and in consideration of relevant international agreements, principles, objectives, and standards, take due account of the need to protect the environment, public health and safety, and generally to conduct their activities in a manner contributing to the wider goal of sustainable development.[436]

The OECD Guidelines add that, in particular, enterprises should establish:

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[424] OECD RBC Guidance above n 370 at 5.
[425] OECD Guidelines above n 370 Commentary on General Policies at para 14.
[426] OECD, *Due Diligence Guidance for Responsible Supply Chain of Minerals from Conflict-Affected Areas*, 2016.
[427] OECD-FAO, *Guidance for Responsible Agricultural Supply Chains*, 2016.
[428] OECD, *Due Diligence Guidance for Responsible Supply Chains in the Garment and Footwear Sector*, 2017.
[429] OECD *Responsible Business Conduct for Institutional Investors: Key Considerations for due diligence under the OECD Guidelines for MNEs*, 2016.
[430] OECD *Due Diligence Guidance for Meaningful Stakeholder Engagement in the Extractive Sector*, 2017.
[431] OECD *Working Party on Export Credits and Credit Guarantees Recommendation of the Council on Common Approaches for Officially Supported Export Credits and Environmental and Social Due Diligence*, April 2016.
[432] Any individual or organisation with a legitimate interest in the matter can submit a case to an NCP regarding a company operating in or from the country of the NCP which has not observed the Guidelines. NCPs provide a mediation and conciliation platform to resolve such disputes concerning the OECD Guidelines.
[433] OECD Guidelines above n 370 Commentary on General Policies at para 14.
[434] Section XI Taxation of the OECD Guidelines ibid at 60.
[435] OECD Guidelines above n 370 Commentary on General Policies at para 14 specifies that the due diligence recommendation of the Guidelines do not apply to the chapters on Science and Technology, Competition and Taxation.
[436] OECD Guidelines above n 370, Section VI Environment.

> [M]easurable objectives and, where appropriate, targets for improved environmental performance and resource utilisation, including periodically reviewing the continuing relevance of these objectives; where appropriate, targets should be consistent with relevant national policies and international environmental commitments.[437]

In addition, the OECD Guidelines provide that enterprises should continually seek to improve corporate environmental performance, at the level of the enterprise and, where appropriate, of its supply chain, by encouraging activities such as, for instance: [438]

> [D]evelopment and provision of products or services that have no undue environmental impacts; are safe in their intended use; reduce greenhouse gas emissions; are efficient in their consumption of energy and natural resources; can be reused, recycled, or disposed of safely.

The Commentary on the Environment of the OECD Guidelines explains, concerning "sound environmental management", that it should be interpreted "in its broadest sense, embodying activities aimed at controlling both direct and indirect environmental impacts of enterprise activities".[439]

The Commentary further states that:

> The basic premise of the Guidelines is that enterprises should act as soon as possible, and in a proactive way, to avoid, for instance, serious or irreversible environmental damages resulting from their activities.[440]

In addition, article 4 of the OECD Guidelines also echoes the precautionary principle[441] by specifying that:

> Consistent with the scientific and technical understanding of the risks, where there are threats of serious damage to the environment, taking also into account human health and safety, not use the lack of full scientific certainty as a reason for postponing cost-effective measures to prevent or minimize such damage.

Furthermore, the OECD Guidelines encourage:[442]

> [D]isclosure or communication practices in areas where reporting standards are still evolving such as, for example, social, environmental and risk reporting. This is particularly the case with greenhouse gas emissions, as the scope of their monitoring is expanding to cover direct and indirect, current and future, corporate and product emissions; biodiversity is another example.

These provisions formed the basis of a specific instance against the financial institution ING before the Dutch OECD National Contact Point (NCP) in relation to the company's climate policy.[443] The parties submitting the notification requested that ING identified and published its total carbon footprint, including its indirect greenhouse gas emissions (as a result of its loans and investments) and established objectives to align its indirect

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437 Ibid at article 1.b.
438 Ibid at article 6.
439 OECD Guidelines ibid, Commentary on the Environment at para 69.
440 Ibid.
441 Discussed below under the subsection entitled "Environmental due diligence".
442 OECD Guidelines ibid, Commentary on Disclosure, Section III.
443 Netherlands National Contact Point for the OECD Guidelines, Final Statement, *Oxfam Novib, Greenpeace Netherlands, BankTrack and Friends of the Earth Netherlands (Milieudefensie) versus ING*, 19 April 2019, available at: file:///C:/Users/User/Downloads/190419-Final+Statement+NGOs-vs-ING.pdf.

emissions with the objectives of the Paris Agreement on climate change.[444] In its final statement, the NCP clarified concrete ways in which companies' individual due diligence actions can include targets to address climate change. In particular, the NCP observed that:[445]

> [T]he OECD Guidelines demand that ING, and other commercial banks, put effort into defining, where appropriate, concrete targets to manage its impact towards alignment with relevant national policies and international environmental commitments. Regarding climate change, the Paris Agreement is currently the most relevant international agreement between states, a landmark for climate change.

Following the NCP procedure, the parties came to an agreement whereby ING committed itself to steer its lending portfolio towards meeting the Paris Agreement's goal well-below 2 degrees, and to set and publish intermediate targets.[446] The final statement issued by the NCP constitutes the first ever NCP case related to climate change due diligence, and is to date the only one.

3.2.3 The ILO Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy (ILO MNE declaration)

The MNE Declaration was adopted by the Governing Body of the ILO in 1977, and amended several times.[447] It is the only global instrument in this field which was jointly elaborated and adopted by governments, employers and workers from around the world.[448]

The principles set out in the MNE Declaration are addressed to multinational corporations, governments employers' and worker's organisations of both home and host countries,[449] and cover areas such as employment, training, conditions of work and life, and industrial relations as well as general policies.[450]

In its most recent revision of March 2017, the MNE aligned with the UNGPs, and provides guidance on due diligence processes in achieving decent work, sustainable businesses, more inclusive growth, and better sharing of the benefits of foreign direct investment ("FDI"), particularly relevant for the achievement of Sustainable Development Goal 8.[451] General Policies 10 provides in particular that:

> Enterprises, including multinational enterprises, should carry out due diligence to identify, prevent, mitigate and account for how they address their actual and potential adverse impacts that relate to internationally recognized human rights, understood, at a minimum, as those expressed in the International Bill of Human Rights and the principles concerning fundamental rights set out in the ILO Declaration on Fundamental Principles and Rights at Work.

It also emphasises the importance of meaningful consultation with potentially affected groups and other relevant stakeholders including workers' organisations in the

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444 UN Paris Agreement on Climate Change (2015), available at: https://unfccc.int/process-and-meetings/the-paris-agreement/d2hhdC1pcy; referenced ibid at 2.
445 Ibid at 5.
446 Ibid at para 5.4.
447 ILO MNE Declaration above n 416.
448 ILO, "What is the ILO MNE Declaration", available at: https://www.ilo.org/empent/areas/mne-declaration/WCMS_570332/lang--en/index.htm.
449 ILO MNE Declaration above n 416, General Policies No 10.
450 Ibid.
451 ILO, "ILO revises its landmark Declaration on multinational enterprises" (17 March 2017), available at : https://www.ilo.org/global/about-the-ilo/newsroom/news/WCMS_547615/lang--en/index.htm.

identification and assessment of actual or potential adverse human rights impacts resulting from companies' own activities or from their business relationships.[452]

3.2.4 Other international standards

Due diligence expectations for adverse human rights and environmental impacts resulting from business activities have started to emerge ever since the Protect, Respect and Remedy Framework for Business and Human Rights (on which the UNGPs were built) was published in 2008. For example, the ISO 26000 standard on corporate social responsibility was launched in 2010, following negotiations between many different stakeholders globally, including governments, NGOs, industry, consumer groups and labour organisations, over a five year period.[453] ISO 26000 "provides guidance on how businesses and organizations can operate in a socially responsible way", notably in the fields of human rights, labour practices, and the environment.[454] Under ISO 26000, organisations are expected to exercise due diligence to avoid contributing to negative impacts through their activities or the activities that are "significantly linked to those of the organization".[455]

The definition of due diligence of ISO 26000 is quite similar to the one of the UNGPs or the OCED Guidelines:[456]

> [C]omprehensive, proactive process to identify the actual and potential negative social, environmental and economic impacts of an organization's decisions and activities over the entire life cycle of a project or organizational activity, with the aim of avoiding and mitigating negative impacts.

Since the UNGPs, other international frameworks have incorporated expectations on due diligence for human rights and environmental impacts, including on climate change. For example, due diligence expectations have been introduced into the International Finance Corporation (IFC) Performance Standards[457] and the Equator Principles (for financial institutions),[458] and various industry standards such as the Voluntary Principles on Security and Human Rights in the extractives sector.[459]

3.2.5 EU-level standards and developments

The EU has instituted a number of initiatives imposing certain due diligence obligations for human rights and environmental impacts, including climate impacts, such as:

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452 ILO MNE Declaration above n 416, General Policies No 10e).
453 International Organization for Standardization ("ISO"), "ISO 26 000 Social Responsibility", available at: https://www.iso.org/iso-26000-social-responsibility.html.
454 Ibid.
455 Ibid, "Guidance on social responsibility".
456 ISO, "ISO 26000 and OECD Guidelines: Practical overview of the linkages" (7 February 2017), available at: https://www.iso.org/files/live/sites/isoorg/files/store/en/PUB100418.pdf.
457 The International Finance Corporation ("IFC") Environmental and Social Performance Standards (2012) "define IFC clients' responsibilities for managing their environmental and social risks", and were revised in 2012 to include references to the UNGPs. Available at: https://www.ifc.org/wps/wcm/connect/Topics_Ext_Content/IFC_External_Corporate_Site/Sustainability-At-IFC/Policies-Standards/Performance-Standards. The 2012 Guidance Notes state that at Guiding Note 1 para 3: "Business should respect human rights, which means to avoid infringing on the human rights of others and address adverse human rights impacts business may cause or contribute to. Each of the Performance Standards has elements related to human rights dimensions that a project may face in the course of its operations. Due diligence against these Performance Standards will enable the client to address many relevant human rights issues in its project." Available at: https://www.ifc.org/wps/wcm/connect/9fc3aaef-14c3-4489-acf1-a1c43d7f86ec/GN_English_2012_Full-Document_updated_June-27-2019.pdf?MOD=AJPERES&CVID=mRQmrEJ.
458 The Equator Principles is a "risk management framework, adopted by financial institutions, for determining, assessing and managing environmental and social risk in projects and is primarily intended to provide a minimum standard for due diligence and monitoring to support responsible risk decision-making", available at: https://equator-principles.com/about/.
459 Voluntary Principles on Security and Human Rights, available at: https://www.voluntaryprinciples.org/.

- The EU Non-Financial Reporting Directive,[460] requires large companies (see below) to publish information on non-financial issues, including the principal risks of adverse human rights and environmental impacts that are linked to the companies' own operations, products and services and business relationships, as well as the policies they pursue around those risks, including the due diligence processes implemented. The Directive applies to public-interest companies of over 500 employees, which covers approximately 6,000 companies across the EU including listed companies, banks, insurance companies and other companies designated by national authorities as public-interest entities.[461]

  The Directive creates a reporting requirement but does not actually require companies to undertake due diligence. In addition, it includes a "comply or explain" mechanism whereby companies may choose not to report by explaining why they are not reporting.

  Member States are required to establish enforcement means to guarantee disclosure, but the Directive gives companies significant flexibility to disclose relevant information. In practice, in the implementation of the EU Non-Financial Reporting Directive by companies in Member States, there seems to be a tendency to focus on the materiality to shareholders rather than risks to those affected.[462]

  On 26 June 2017, the European Commission published its Non-Binding Guidelines,"to help companies disclose relevant non-financial information in a more consistent and more comparable manner".[463]

- Also accompanying the EU non-financial reporting Directive is the recently published Non-Binding Guidelines on corporate climate-related information reporting, which indicate that "climate-related information can be considered to fall into the category of environmental matters".[464] The Guidelines state:

  > [C]ompanies and financial institutions need to better understand and address the risks of a negative impact on the climate resulting from their business activities, as well as the risks that climate change poses to their business.

  The Guidelines further state that:

  > Under the Non-Financial Reporting Directive, climate-related information should, to the extent necessary, include both the principal risks to the development, performance and position of the company resulting from climate change, and the principal risks of a negative impact on the climate resulting from the company's activities. The proposed disclosures in these guidelines reflect both these risk perspectives.[465]

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[460] Directive 2014/95/EU of the European Parliament and of the Council of 22 October 2014 ("EU Non-Financial Reporting Directive").
[461] European Commission, "Non-financial reporting: EU rules require large companies to publish regular reports on the social and environmental impacts of their activities", available at : https://ec.europa.eu/info/business-economy-euro/company-reporting-and-auditing/company-reporting/non-financial-reporting_en#companies-that-must-comply.
[462] See for instance Claire Jeffrey, "Comparing the Implementation of the EU Non-Financial Reporting Directive in the UK, Germany, France and Italy", *Frank Bold*, November 2017, available at: http://www.purposeofcorporation.org/comparing-the-eu-non-financial-reporting-directive.pdf at 4.
[463] EU Non-Binding Guidelines on non-financial reporting (methodology for reporting non-financial information), 2017/C 215/01 of June 2017.
[464] EU Guidelines on non-financial reporting: Supplement on reporting climate-related information, C/2019/4490 of June 2019. See also European Commission, "Sustainable finance: Commission publishes guidelines to improve how firms report climate-related information and welcomes three new important reports on climate finance by leading experts" (18 June 2019), available at: http://europa.eu/rapid/press-release_IP-19-3034_en.htm.
[465] Ibid at para 2.3.

> Unless otherwise stated in the text, references to risks should be understood to refer both to risks of negative impacts on the company (transition risks and physical risks – see below) and to risks of *negative impacts on the climate*.
>
> Both of these kinds of risk – risks of negative impacts on the company and risks of negative impacts on the climate – may arise from the companies own operations and may occur *throughout the value chain*, both upstream in the supply-chain and downstream. [Our emphasis]

The Guidelines also specify that:

> When reporting on their climate-related risks, dependencies and opportunities, companies should, where relevant and proportionate, consider their whole value chain, both upstream and downstream. For companies involved in manufacturing activities this means following a product life cycle approach that takes account of climate issues in the supply chain and the sourcing of raw material, as well as during the use of the product and when the product reaches end-of-life. Companies providing services, including financial services, will also need to consider the climate impacts of the activities that they support or facilitate.[466]

- The EU Timber Regulation ("EUTR"),[467] entered into force in March 2013 and is part of a broad set of measures introduced by the Forest Law Enforcement, Governance and Trade ("FLEGT") Action Plan adopted in 2003 to tackle illegal logging in the world's forests.[468] The EUTR requires operators who place timber and timber products on the EU market to develop or use a due diligence system to assess the risk that timber has been logged or traded illegally, which involves gathering information on timber they want to import, evaluating the probability that it is legal, and taking steps to mitigate the risk of importing illegal timber. A failure to carry out proper due diligence is an offence, even if the wood itself is not shown to be illegal. A recent report on the implementation of the EUTR noted that it is "the first legal instrument at European Union level which includes mandatory due diligence, a key principle for corporate sustainable responsibility in line with the United Nations Guiding Principles on Business and Human Rights (UNGPs)".[469]

- The EU Conflict Minerals Regulation,[470] which will come into force on 1 January 2021, requires EU importers of tin, tantalum, tungsten and gold to follow a five-step framework to: 1) establish strong company management systems; 2) identify and assess risk in the supply chain; 3) design and implement a strategy to respond to identified risks; 4) carry out an independent third-party audit of supply chain due diligence; and 5) report annually on supply chain due diligence.

- The EU Regulation on disclosures relating to sustainable investments and sustainability risks: The Council and Parliament have reached political agreement on a new regulation on sustainability-related disclosures in the financial services

[466] Ibid.
[467] EU Regulation No 995/2010 of the European Parliament and of the Council of 20 October 2010 laying down the obligations of operators who place timber and timber products on the market, , COM(2018) 669 ("EU Timber Regulation").
[468] EU Forest Law Enforcement, Governance and Trade (FLEGT) Facility, "What is the EU FLEGT Action Plan?", available at: http://www.euflegt.efi.int/flegt-action-plan.
[469] EU Timber Regulation above n 467 at para 2.
[470] The EU Proposal for a Regulation of the European Parliament and of the Council setting up a Union system for supply chain due diligence self-certification of responsible importers of tin, tantalum and tungsten, their ores, and gold originating in conflict-affected and high-risk areas, COM/2014/0111 final - 2014/0059 (COD), ("EU Conflict Minerals Regulation").

sector, which forms part of the EU's Action Plan on Financing Sustainable Growth.[471] The regulation introduces disclosure obligations for financial market participants and financial advisers on their approaches to the integration of sustainability risks and the consideration of adverse sustainability impacts, including due diligence policies pursued where they consider principal adverse impacts of investment decisions on sustainability factors.[472]

- The General Data Protection Regulation ("GDPR"):[473] requires the exercise of due diligence with regard to one specific human rights impact: the right to privacy. The GDPR applies to the processing of personal data by EU-based companies, regardless of whether the processing takes place in the EU, as well as to the processing of personal data of data subjects who are in the EU by a non-EU company, where the processing activities are related to goods or services offered in the EU; or the monitoring of their behaviour as far as their behaviour takes place within the EU.

In addition to the above, including the EU Timber Regulation and the EU non-binding guidance on disclosure of climate-related information, in the area of environmental law, the EU has also introduced various regulatory requirements which do not expressly require "due diligence", but are nevertheless relevant for current purposes:

- The EU Environmental Liability Directive[474] requires relevant companies to take (a) all practicable steps to immediately control, contain, remove or otherwise manage the relevant contaminants and/or other damage factors in order to limit or to prevent further environmental damage and adverse effects on human health, and (b) the necessary remedial measures. It does not necessarily require fault or negligence to establish liability, but does provide for companies which can demonstrate an absence of fault or negligence to escape the costs of remedial actions in specific circumstances.

- The Seveso III Directive[475] requires industrial establishments where dangerous substances are used or stored in large quantities to put in place safety measures to prevent major accidents in industrial installations. Relevant companies are required to take all necessary measures to prevent major accidents and to limit their consequences for human health and the environment, which includes notification of all concerned establishments,[476] deploying a major accident prevention policy,[477] producing a safety report for upper-tier establishments,[478]

[471] Proposal for a Regulation of the European Parliament and of the Council on disclosures relating to sustainable investments and sustainability risks and amending Directive (EU) 2016)2341.
[472] Ibid at article 3gamma entitled "Transparency of adverse sustainability impacts at entity level", provides in particular that: 1. Financial market participants shall publish and maintain on their websites either of the following: a) where they consider principal adverse impacts of investment decisions on sustainability factors, a statement on due diligence policies with respect to these principal adverse impacts, taking due account of their size, nature and scale of their activities and the types of their financial products; b) where they do not consider adverse impacts of investment decisions on sustainability factors, clear reasons for not doing so, and, where relevant, including information as to whether and when they intend to consider such adverse impacts. 2. Information provided in accordance with point (a) of the paragraph 1 shall include at least the following: a) information on policies on the identification and prioritisation of principal adverse sustainability impacts and indicators; b) a description of the principal adverse sustainability impacts and of the actions taken and, where relevant, planned; c) brief summaries of engagement policies in accordance with Article 3g of Directive 2007/36/EC, where applicable; d) reference to the adherence to responsible business conduct codes and internationally recognised standards for due diligence and reporting and, where relevant, the degree of alignment with the long-term global warming targets of the Paris Climate Agreement.
[473] Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC, OJ L 119, 4.5.2016 ("EU GDPR"), at 1-88.
[474] EU Directive 2004/35/EC.
[475] EU Directive 2012/18/EU.
[476] Ibid at article 7.
[477] Ibid at article 8.
[478] Ibid at article 10.

producing internal emergency plans for upper tier establishments,[479] and providing information in case of accidents.[480]

- The Directive of the protection of the environment through criminal law[481] applies to Member States and does not establish due diligence requirements, but is relevant mostly insofar as it requires criminal oversight by public bodies at Member State level. Moreover, it was introduced on the basis that:[482]

  > The available information shows that there are large differences between the criminal sanctions provided for environmental offences in the Member States. The existing criminal sanctions are not sufficiently stringent to ensure a high level of environmental protection throughout the Community.

- Although not legally binding, the European Commission's Organisation Environmental Footprint (OEF) is a multi-criteria measure of the environmental performance of a goods or services providing organisation from a life cycle perspective.[483] It requires relevant companies to monitor and communicate their performance based on a comprehensive assessment of environmental impacts over the life cycle. It is particularly relevant to this study insofar as it focuses on the life cycle of value chain of goods and services, and includes the ongoing monitoring and communication aspects of the concept of due diligence.

- Similarly, the EU Eco-Management and Audit Scheme is a voluntary "management instrument" for companies to "evaluate, report, and improve their environmental performance".[484] It applies worldwide and across sectors. It requires companies to perform an environmental review constituted of five main parts, the first of which, reminiscent of the impact assessment described in the UNGPs and OECD Guidelines, is determination of the organisational context. It should cover such issues as climate, air quality, water quality, natural resources availability and biodiversity, as well as cultural, social and political circumstances. The review also includes determination of the "needs and expectations" of interested parties such as employees, shareholders, and suppliers, including their needs and expectations.[485]

In addition to the existing measures at the EU level, calls for an EU-level legislation on mandatory human rights and environmental due diligence across sectors and across commodities have started to emerge, both from NGOs and trade unions[486] and from certain major multinational corporations.[487] In its *Shadow EU Action Plan* released in March 2019, the Responsible Business Conduct Working Group (RBC Group) of the European Parliament called, *inter alia*, for the adoption of mandatory due diligence for

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[479] Ibid at article 12.
[480] Ibid at article 16.
[481] EU Directive 2008/99/EC on the protection of the environment through criminal law.
[482] European Commission DG Environment, "Combating Environmental Crime", available at: https://ec.europa.eu/environment/legal/crime/index.htm.
[483] European Commission "Organisation Environment Footprint Guide", Deliverable 3 and 4B to the Administrative Arrangement between DG Environment and Joint Research Centre No. N 070307/2009/552517, including Amendment No 1 from December 2010, available at: https://ec.europa.eu/environment/eussd/pdf/footprint/OEF%20Guide_final_July%202012_clean%20version.pdf. See also the European Commission "Organization Environmental Footprint and the Development of Sector-Specific Guidance Documents", available at: https://ec.europa.eu/jrc/en/publication/ec-organization-environmental-footprint-and-development-sector-specific-guidance-documents.
[484] European Commission DG Environment "Eco-Management and Audit Scheme", available at: https://ec.europa.eu/environment/emas/index_en.htm.
[485] The organisation can decide to voluntarily fulfil these needs or expectations. It is noted that these are voluntary additional considerations, whereas in due diligence the role of stakeholders engagement is central to the concept.
[486] European Coalition for Corporate Justice ("ECCJ"), "Civil Society Calls for Human Rights and Environmental Due Diligence Legislation", 3 October 2019, available at: http://corporatejustice.org/news/16785-civil-society-calls-for-human-rights-and-environmental-due-diligence-legislation.
[487] Fern, "Chocolate companies and MEPs call for EU Due Diligence Regulation", 10 April 2019, available at: https://www.fern.org/news-resources/chocolate-companies-and-meps-call-for-eu-due-diligence-regulation-954/.

EU businesses and business operating within the EU.[488] On 3 October 2019, over 80 NGOs and trade unions published a call on the European Commission "for effective EU legislation that establishes a mandatory human rights and envrionmental due diligence framework for business, companies and financial institutions operating, or offering products or service, within the EU".[489]

3.2.6 Domestic measures regulating due diligence in supply chains

Various domestic legislative measures address supply chain due diligence, but they are often sector- or issue-specific. These are discussed in further detail in the country reports and the analysis of the country reports below, but herewith a brief overview.

- The 2017 French Duty of Vigilance law[490] is the only legislative example to date which imposes a general mandatory due diligence requirement for human rights and environmental impacts. The law imposes a duty of vigilance on certain large French companies (employing 5000 employees in France, or 10,000 globally). The law extends to the activities of French companies' subsidiaries and subcontractors and business enterprises in the supply chain "with which the company maintains an established commercial relationship". In order to discharge their legal duty, companies need to implement a "vigilance plan" which should include reasonable measures to adequately identify risks and prevent serious violations of human rights and the environment. As this law is new, there are not yet any court decisions to clarify how this law will be applied, with valuable analysis in the France Country Report in this Section being important. However, during the course of this study various legal actions were instituted in terms of this law.[491]

- The Dutch Child Labour Due Diligence Law was passed in May 2019.[492] It applies to issues of child labour in supply chains for all companies (Dutch and others) operating in the Netherlands. Companies will be required to issue a statement declaring that they have exercised due diligence to prevent their goods and services being made using child labour. As this law has just been passed, there is

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488 Shadow EU Action Plan above n 394 at 6.
489 ECCJ above n 486.
490 French Law No. 2017-399 of March 27, 2017 on the "Duty of Care of Parent Companies and Ordering Companies".
491 For example, the following formal notices have been sent: 1) A formal notice was sent to Total on 19 June 2019 by French NGOs (Sherpa, Notre Affaire à Tous), Ecomaires as well as 14 local authorities requesting Total to update its vigilance plan with respect to its climate change impacts on the basis of the French Duty of Vigilance Law.Notre Affaire A Tous, Sherpa, Les Eco Maires & ZEA "1,5°C: 13 French Local Authorities and 4 NGOs ask the French oil company Total to prevent global warming", 23 October 2019, available at: https://notreaffaireatous.org/wp-content/uploads/2018/10/DP-english.pdf; 2) Another formal notice was sent to Total on 25 June 2019 by French NGO les Amis de la Terre and Ugandan NGOs for allegedly failing to meet the requirements of the Act with respect to the company's impacts on local communities in Uganda. Environment News Service (ENS), "Total Sued Under France's New Duty of Vigilance Law" (23 October 2019), available at: http://ens-newswire.com/2019/10/23/total-sued-under-frances-new-duty-of-vigilance-law/; AFP, "NGOs file suit against Total over Uganda oil project", *The East African* (24 October 2019), available at: https://www.theeastafrican.co.ke/business/NGOs-sue-Total-over-Uganda-oil-project/2560-5323092-r3aeku/index.html. See also BHHRC, "14 Cities and NGOs call on Total to comply with French Duty of Vigilance Law", available at: https://www.business-humanrights.org/en/14-cities-ngos-call-on-total-to-comply-with-french-duty-of-vigilance-law; 3) On 18 July 2019, a formal notice was sent to Teleperformance by French NGO Sherpa and international trade union UNI Global Union to comply with its vigilance obligations in relations to workers' rights and freedom of association in its subsidiaires. Sherpa, "Sherpa and UNI Global Union send formal notice to Teleperformance calling on the world leader in call centers to strenghten workers' rights", 24 July 2019, available at: https://www.asso-sherpa.org/sherpa-and-uni-global-union-send-formal-notice-to-teleperformance-calling-on-the-world-leader-in-call-centers-to-strengthen-workers-rights-2; 4) On 26 September 2019, indigenous human rights defenders, Mexican NGO ProDESC, and the European Centre for Constitutional and Human Rights (ECCHR) sent a formal notice to EDF calling on the company to comply with its duty of vigilance with respect to a wind farm project in the State of Oaxaca. ProDESC, "Indigenous human rights defenders and NGOs call on EDF Group to comply with its duty of vigilance regarding human rights prescribed by the French 'Duty of Vigilance' Law", 15 November 2019, available at: https://prodesc.org.mx/indigenous-human-rights-defenders/; 5) On 1 October 2019, a formal notice was sent by the international trade unions International Transport Workers' Federation ("ITF"), the European Transport Workers' Federation ("ETF") and an alliance of unions to XPO Logistics Europe for allegedly failing to meet the requirements of the law in relations to labour issues in its supply chain. ITF, "Transport giant served notice under duty of vigilnce law in landmark legal move", 1 October 2019, available at: https://www.itfglobal.org/en/news/transport-giant-served-notice-under-duty-vigilance-law-in-landmark-legal-move.
492 Netherlands *Kamerstukken I*, 2016/17, 34 506, A ("Dutch Child Labour Due Diligence Law"). See for the original version: *Kamerstukken II*, 2015/16, 34 506, nr. 2.

limited discussion of it, though there is valuable analysis in the Netherlands Country Report in this Section.

Some relevant legal proposals to impose a similar general duty at domestic level:

- In Switzerland there is currently a popular initiative and legislative counter-proposals for a mandatory due diligence law.[493] The Finland government has committed to consider such a law.[494] Preliminary political steps have also been taken in Denmark, where a parliamentary motion calling for the introduction of a bill on human rights due diligence is currently under consideration.[495] In Germany, an unofficial draft paper is circulating amongst stakeholders which outlines a possible mandatory due diligence law,[496] and the German National Action Plan indicated that regulation will be considered if a currently ongoing survey shows that less than 50% of companies are implementing due diligence.[497] In December 2019, it was announced that a draft outline for a German "supply chain Act" will be published in 2020.[498] In addition, the Italian Government committed to assess legislative reform introducing human rights due diligence.[499] The UK Joint Committee on Human Rights has also proposed that a "failure to prevent adverse human rights impacts" mechanisms be considered for corporate human rights abuses.[500]

- Civil society campaigns have called for mandatory due diligence laws in Austria, Belgium, Italy, Luxembourg, the Netherlands, Norway, Sweden and the UK.[501]

Other legislations do not expressly impose due diligence requirements on companies but incentivise the adoption of due diligence processes:

- The Italian Legislative Decree 231/2001[502] establishes corporate liability for crimes committed in the interest or to the benefit of a legal entity, which includes specific human rights violations such as slavery, human trafficking, forced labour, juvenile prostitution and pornography, female genital mutilation, serious bodily harm resulting from a breach of health and safety standards, and environmental crimes.[503] The law itself does not expressly require the exercise of due diligence requirements for human rights and environmental impacts, but creates a defence against corporate liability for the above offences if the company can show that it

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[493] Swiss Coalition for Corporate Justice ("SCCJ"), "The Initiative Text with Explanations", available at: https://corporatejustice.ch/wp-content/uploads//2018/06/KVI_Factsheet_5_E.pdf; SCCJ, "How does the parliamentary counter-proposal differ from the popular initiative (RBI)?", May 2018, available at: https://corporatejustice.ch/wp-content/uploads/2018/07/Comparision_RBI_counter-proposal_EN-1.pdf.

[494] See Ykkösketjuun official website available at: https://ykkosketjuun.fi/en/.

[495] BHRRC above n 118.

[496] BHRRC, "German Development Ministry drafts law on mandatory human rights due diligence for German companies", available at: https://www.business-humanrights.org/en/german-development-ministry-drafts-law-on-mandatory-human-rights-due-diligence-for-german-companies. It is noted that the German Federal Government recently issued a statement stressing that the document merely constitutes "internal considerations" within the German Federal Ministry for Industrial Cooperation and Development ("BMZ"), https://www.bundestag.de/presse/hib/670510-670510.

[497] German Federal Foreign Office, "National Action Plan: Implementation of the UN Guiding Principles on Business and Human Rights 2016-2020" (September 2017), 10, available at: https://www.auswaertiges-amt.de/blob/610714/fb740510e8c2fa83dc507afad0b2d7ad/nap-wirtschaft-menschenrechte-engl-data.pdf.

[498] Manfred Shäfers "Regiering droht mit einem Lieferkettengesetz", *Frankfurter Allgemeine*, 11 December 2019; Caspar Dohmen, "Minister arbeiten an Lieferkettengesetz", *Süddeutsche Zeitung*, 11 December 2019.

[499] BHRRC above n 118.

[500] UK Joint Committee on Human Rights, *Human Rights and Business 2017: Promoting Responsibility and Ensuring Accountability*, April 2017 available at: https://publications.parliament.uk/pa/jt201617/jtselect/jtrights/443/443.pdf.

[501] BHRRC above n 118.

[502] Decreto Legislativo 8 giugno 2001, n. 231, *Disciplina della responsabilità amministrativa delle persone giuridiche, della società e delle associazioni anche prive di personalità giuridica*, a norma dell'articolo 11 della legge 29 settembre 2000, n. 300, pubblicato nella Gazzetta Ufficiale n. 140 del 19 giugno 2001. See Regulatory Review and Italy Country Report.

[503] FIDH, HRIC and ECCJ, "Italian Legislative Decree No. 231/2001: A model for Mandatory Human Rights Due Diligence Legislations?", November 2019, available at: https://e6e968f2-1ede-4808-acd7-cc626067cbc4.filesusr.com/ugd/6c779a_d800c52c15444d74a4ee398a3472f64c.pdf at 10.

adopted "models of organisation, management and control" in order to identify, prevent and mitigate the risk of commission of the relevant crime.

Some legislative measures require reporting requirements with respect to certain human rights only, such as modern slavery and forced labour:

- The 2010 California Transparency in Supply Chains Act (the "California Act"),[504] requires certain companies to report on their specific actions to eradicate slavery and human trafficking in their supply chains. However, a 2015 Report found that the "average disclosure compliance score" under the Act was 60%, and the average "affirmative conduct score" relating to "the extent of corporate-driven action" was 31%.[505]

- The UK Modern Slavery Act 2015 requires companies with a certain turnover[506] carrying out "business or part of a business" in the UK[507] to report annually on the steps the company has taken, if any, to ensure that slavery and human trafficking has not taken place in its supply chains or in its own business (or to report if no steps have been taken).[508] However, it does not mandate what should be reported in the statement,[509] and falls short of prescribing a positive obligation to undertake due diligence. It also only relates to steps taken in relation to slavery, forced labour and human trafficking, thereby not including due diligence for other human rights or environmental impacts.[510] Both the UK and the California Act allows companies to state that they have taken no steps to address modern slavery in their supply chains.[511]

- In 2018 Australia introduced a Modern Slavery Act, largely modelled on the UK Act, with broader application (such as including government obligations to report).[512] Similar legislation regulating modern slavery in supply chains have been proposed in New Zealand[513] and Hong Kong, [514] and in New South Wales in Australia.[515]

Anti-corruption laws often require due diligence through the supply chain, and failure to exercise this could be a criminal offence, also exposing individual directors to criminal liability. For example, the US Foreign Corrupt Practices Act,[516] and the UK Bribery Act 2010 will often be the frame of reference for companies when speaking about compliance with "due diligence" requirements.

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504 California Transparency in Supply Chains Act of 2010.
505 Development International "Corporate Compliance with the California Transparency in Supply Chains Act of 2010" (2 November 2015), available at: http://media.wix.com/ugd/f0f801_0276d7c94ebe453f8648b91dd35898ba.pdf at 2.
506 The UK Modern Slavery Act 2015 applies to companies with a global annual turnover of £36m or more.
507 Section 54(12) of UK Modern Slavery Act ibid.
508 Section 54 of the UK Modern Slavery Act ibid.
509 However, the UK Government Guidance suggests six areas of reporting. UK Government, "Slavery and human trafficking in supply chains: guidance for businesses", available at: https://www.gov.uk/government/publications/transparency-in-supply-chains-a-practical-guide. See also "Independent Review of the UK Modern Slavery Act 2015, Final Report", 22 May 2019, available at: https://www.gov.uk/government/publications/independent-review-of-the-modern-slavery-act-final-report at 15.
510 Chiara Macchi and Claire Bright, "Hardening Soft Law: The Implementation of Human Rights Due Diligence Requirements in Domestic Legislation", in M. Buscemi, N. Lazzerini and L. Magi, *Legal Sources in Business and Human Rights - Evolving Dynamics in International and European Law* (forthcoming, Brill, 2019).
511 NYU Stern Center for Business and Human Rights, "Research Brief: Assessing Legislation on Human Rights in Supply Chains: Varied Designs but Limited Compliance" (19 June 2019), available at: https://issuu.com/nyusterncenterforbusinessandhumanri/docs/nyu_jaco_research_brief_june14_fina at 5.
512 Australian Modern Slavery Act 2018.
513 The New Zealand Transparency in Supply Chains Bill, 2017, available at: https://www.parliament.nz/en/pb/bills-and-laws/proposed-members-bills/document/52HOH_MEMBILL048_1/transparency-in-supply-chains-bill.
514 Norton Rose Fulbright "Modern Slavery And Human Trafficking – A Comparative Analysis Of Existing And Emerging Legislation In The United Kingdom, Australia, Hong Kong And Singapore", March 2018, available At: http://www.nortonrosefulbright.com/knowledge/publications/165269/modern-slavery-and-human-trafficking-a-comparative-analysis-of-existing-and-emerging-legislation-in-the-unit.
515 New South Wales Modern Slavery Act 2018 No 30.
516 US Foreign Corrupt Practices Act 15 USCs78dd-1 (1977).

Other legislative measures which require supply chain due diligence focus on other human rights issues, frequently labour-related, such as the US Trade Facilitation Act which allows US Customs to seize imported goods if an importer is unable to provide a certificate proving which measures were taken ensure that the goods were not produced using forced labour,[517] or the Netherlands Child Labour Due Diligence Act which requires companies to conduct due diligence in order to address the risk of child labour in their own operations and in their supply chains (discussed above).[518]

Some examples also exist for supply chain due diligence requirements limited to specific sectors, such as:

- the timber sector,[519]
- industries which extract and use potential conflict minerals,[520]
- and food safety.[521]
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A number of countries also have due diligence requirements relating to product safety. For instance, it is noted in the Finnish Country Report that in Finland:[522]

> Companies are required to ensure that the products they sell are safe for consumers and users. This includes an obligation to conduct duty of care on whether the products can cause danger to health or property of the consumer and in an extent that is reasonable in relation to the circumstances and professional ability. Due diligence in the broad sense includes that the operator must provide adequate information to consumers in their marketing so that consumers can evaluate the associated hazards of consumer goods and consumer services. The Supervisory Authority, Finnish Safety and Chemicals Agency, can require operators to give consumers information in a suitable way on the prevention or prevention of the risks associated with the use or operating instructions necessary.

Following the implementation of EU Directives on public procurement, a number of EU Member States have also included human rights and environmental due diligence requirements in their national laws relating to public procurement.

- For instance, the Denmark Country Report explains that the Local Government Purchasing Service (SKI)'s framework agreements:[523]

  > [I]nclude requirements to the suppliers to exhibit due diligence in relation to child labour, forced labour freedom of association, gender discrimination, migrant labour and other areas across different sectors and categories. In respect to this requirement suppliers are obligated to investigate human rights risks in connection to their business activities in relation to themselves and other companies they might influence, such as major subcontractors. Simultaneously suppliers are obligated to take measures to prevent the risks. The purpose of the provisions is for

[517] BHRRC, "Modern Slavery in Company Operations and Supply Chains: Mandatory transparency, mandatory due diligence and public procurement due diligence" (September 2017) at 18.
[518] Dutch Child Labour Due Diligence Law above n 483.
[519] For example, the US Lacey Act of 190, 16 USC s3372(a)(2(A) (2006); and the Australia Illegal Logging and Prohibition Act 2012 (Cth).
[520] For example, section 1502 of the US Dodd-Frank Act. See also Galit A Safarty "Shining A Light on Global Supply Chains" 56 *Harvard International Law Journal* 419 at 423.
[521] For example, article 18 of the EU General Food Law Regulation (EC) No. 178/2002; and UK Guidance notes, Food safety, traceability, product withdraw and recall: General Food Law Regulation guidance for food businesses - Guidance Notes on Articles 14, 16, 18 and 19 of the General Food Law Regulation (EC) No. 178/2002; and EU Guidance on the Implementation of Articles 11, 12, 16, 17, 18, 19 And 20 Of Regulation (Ec) 178/2002 on General Food Law (20 December 2004), available at: https://www.food.gov.uk/sites/default/files/multimedia/pdfs/1782002euguidance.pdf.
[522] See Finland Country Report.
[523] See Denmark Country Report.

instance to ensure decent work and environmental conditions in relation to the production of the products, which are purchased by the public institutions. The agreements include requirements to the suppliers to demonstrate social responsibility by adhering to a set of requirements that are based on internationally recognized principles and international initiatives, such as UN Global Compact, UN Guiding Principles on Business and Human Rights, and OECD Guidelines for Multinational Enterprises.

- The Ireland country reports quotes the Baseline Assessment according to which:[524]

> [H]uman rights due diligence ought to be considered as a minimum requirement for State companies, businesses that obtain government contracts through the public procurement process, businesses that Ireland engages with through its embassies and State agencies and bodies that derive State support and that act outside the jurisdiction. Human rights due diligence should include reporting on human rights practices outside the jurisdiction so that companies that provide human rights reporting in Ireland, whether due to being domiciled in Ireland, or otherwise, must also report on the human rights of their out of territory operations.

Some countries have due diligence requirements relating to director's duties.

- For instance, the UK country report notes that:[525]

> Whilst directors are obliged under section 172 of the Companies Act to have regard to employees, the community and the environment in carrying out their functions, this is ultimately within the context of a broader fiduciary duty to promote the success of the company for the benefit of the members as a whole. In other words, the company's (and shareholders') interests have primacy.

- The Netherlands country report explains that under certain circumstances, directors of Dutch companies have a duty to exercise due care with respect to the interests of "external" stakeholders which "means that they may need to refrain from doing things that would unnecessarily or unduly harm those interests".[526]

Some examples of non-regulatory standards due diligence standards include:

- The Canadian Ombudsperson for Responsible Enterprise ("CORE") has a mandate to investigate allegations of human rights abuses linked to Canadian corporate activity abroad.[527]

- Where governments use their purchasing power[528] to effect change in the private sector by integrating human rights and labour standards into the public procurement process. For example, the EU rules on public procurement and concession contracts directly address the use of subcontractors by suppliers.[529] Public procurement requirements may also be limited to specific sectors, such as

[524] See Ireland Country Report.
[525] Se UK Country Report.
[526] See Netherlands Country Report.
[527] Global Affairs Canada, "Responsible business conduct abroad - Questions and answers", available at: https://www.international.gc.ca/trade-agreements-accords-commerciaux/topics-domaines/other-autre/faq.aspx?lang=eng.
[528] For example, see UK Joint Committee on Human Rights above n 500 at 30.
[529] For example, EU Directive 2014/24/EU on public procurement and repealing Directive 2004/18/EC; and see Olga Martin-Ortega, Opi Outhwaite and Willam Rook "Buying Power and Human Rights in the Supply Chain: legal options for socially responsible public procurement of electronic goods" 19(3) *The International Journal of Human Rights* 341 at 352-3 and 347.

the private security sector,[530] or to certain human rights issues, such as human trafficking[531] or working conditions.[532] A 2016 survey of the public procurement practices in 20 jurisdictions suggests that the power of public procurement has been largely under-utilised for the purposes of due diligence for human rights and environmental impacts by most states to date.[533]

3.2.7 Case law

As there is currently no general duty on companies to undertake due diligence for their human rights and environmental harms in most EU jurisdictions,[534] case law has developed various possible avenues to bring such claims for both corporate human rights and environmental harms.[535]

Many of the cases to date are brought in terms of tort law.[536] The Office of the High Commissioner for Human Rights (OHCHR) noted that: "the concept of negligence is a basis for corporate liability in many jurisdictions" and that "the extent to which a company conducts human rights due diligence can be relevant when determining whether it negligently caused or contributed to harm."[537] Civil law cases are often brought against a parent company for harms which took place through the activities of its subsidiary, and raise questions of parent company liability and duty of care.[538] For instance, courts in Canada,[539] the Netherlands,[540] the UK[541] and Sweden[542] have been willing to assume jurisdiction over cases where human rights and/or environmental harms have occurred outside the home state by subsidiaries of the defendant parent company. In other jurisdictions such as France, legal proceedings have also raised the question of the parent company liability for the harm caused to the employees of its subsidiaries, although the discussions have taken place through the concept of co-employer.[543] Some of these tort cases are yet to be decided before a trial court.

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[530] The International Code of Conduct for Private Security Providers' Association ("ICoCA") is a multi-stakeholder initiative which sets out a code of conduct for private security companies. Member States commit to require their private security providers to abide by the Code.
[531] For example, the US Federal Acquisition Regulation Subpart 22.17 and Part 52 (2012). See also Hogan Lovells, "Contractors and Companies in the federal supply chain have an opportunity to prepare for the impending, significant explosion of the government's anti-human trafficking rules" (6 March 2014), available at: https://www.lexology.com/library/detail.aspx?g=ccb6302b-03ff-4744-9a0e-fbb1c65dff39.
[532] International Learning Lab on Public Procurement and Human Rights, "Public Procurement and Human Rights: A Survey of Twenty Jurisdictions" (July 2016), available at: https://www.hrprocurementlab.org/wp-content/uploads/2016/06/Public-Procurement-and-Human-Rights-A-Survey-of-Twenty-Jurisdictions-Final.pdf at 42.
[533] Ibid.
[534] Although this exists in other jurisdictions, such as South Africa, where the Bill of Rights applies to private actors. See Constitution of the Republic of South Africa Act 108 of 1996.
[535] It is noted that examples of reported cases that simply deal with corporate environmental law compliance without reference to any due diligence or related requirements or failures fall outside of the scope of this study.
[536] For an overview of the cases of corporate human rights abuses committed in third countries filed before EU Member States see Axel Marx, Claire Bright and Jan Wouters, "Access to Legal Remedies for Victims of Coporate Human Rights Abuses in Third Countries", 2019, available at: http://www.europarl.europa.eu/RegData/etudes/STUD/2019/603475/EXPO_STU(2019)603475_EN.pdf.
[537] OHCHR, "Improving accountability and access to remedy for victims of business-related human rights abuse: the relevance of human rights due diligence to determinations of corporate liability", UN Doc. A/HRC/38/20/Add.2 (1 June 2018) at 19.
[538] See for instance Dalia Palombo, "The Duty of Care of the Parent Company: A Comparison between French Law, UK Precedents and the Swiss Proposals", *Business and Human Rights Journal*, 2019, 1; Claire Bright, "The Civil Liability of the Parent Company for the Acts or Omissions of Its Subsidiary: The Example of the Shell Cases in the UK and in the Netherlands", in Angelica Bonfanti (ed.) *Business and Human Rights in Europe: International Law Challenges* (Routledge, 2018) 212.
[539] *Choc v Hudbay Minerals Inc* [2013] ONSC 1414); *Garcia v Tahoe Resources* (2017 BCCA 39); *Hill v Hamilton- Wentworth Regional Police Services Board* 2007 SCC 41 at [20].
[540] *Akpan v Royal Dutch Shell PLC* Arrondissementsrechtbank Den Haag, 30 January 2013 Case No C/09/337050/HA ZA 09-1580.
[541] For example, *Vedanta Resources PLC and another v Lungowe and others*, [2019] UKSC 20. See also the UK Country Report.
[542] Rasmus Kløcker Larsen, "Foreign Direct Liability Claims in Sweden: Learning from *Arica Victims KB v. Boliden Mineral AB*?" 83 *Nordic Journal of International Law*, 2014, 404.
[543] Nicolas Bueno, "Multinational enterprises and labour rights: concepts and implementation", in Janice R Bellace and Beryl ter Haar, *Research Handbook on Labour, Business and Human Rights Law*, 421 at 429.

A number of criminal law proceedings have been filed in various Member States such as France,[544] Germany,[545] and the Netherlands[546] against a parent company or its managers for being complicit in human rights abuses,[547] one of which resulting in the conviction of the CEO of Oriental Timber Company by the Dutch Supreme Court on 18 December 2018 for aiding and abetting war crimes.[548]

Both civil and criminal law proceedings have given rise to a number of concerns around the issue of effective access to justice and remedies for victims of corporate human rights and environmental harms.[549] A recent academic study mapped out the legal proceedings brought in Europe against EU-based companies on the basis of human rights and environmental abuses in third countries over the last decade. Of the 38 cases analysed, 14 were dismissed, 19 are still ongoing, 4 were fully settled out of court and only 1 led to a successful judicial outcome for the claimants on the merits of the case.[550]

Other claims have been based on specific statutory obligations, such as laws about human trafficking,[551] and consumer protection laws. For instance, legal proceedings on the basis of deceptive commercial practices were instituted in Germany[552] and in France[553] on the basis of the alleged discrepancies between companies' public statements or advertising campaigns and the reality of the working conditions in their supply chains.[554]

Certain claims have been brought in terms of directors' duties. For instance, the Finland country reports a decision of the Supreme Court of Finland in which it was held that "the negligence of two members of a three member Board of Directors was gross considering that they had not familiarized themselves with the content of the environmental permit". The court also ruled that "they had deliberately neglected their duty to arrange and supervise matters related to the permit".[555]

Increasingly, but still in very few cases to date, claims are being instituted against companies for failing to disclose climate-related risks.[556] Other cases are challenging companies' decisions on the basis that they allegedly pose unjustifiable financial (climate-related) risks to their shareholders.[557] For example, the Polish District Court of Poznán held that the resolution of the Polish energy company Enea to authorise construction of a coal power plant (a joint venture between Enea and Energa) was

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[544] See for instance BHRRC, "Lafarge lawsuit (re complicity in crimes against humanity in Syria", available at: https://www.business-humanrights.org/en/lafarge-lawsuit-re-complicity-in-crimes-against-humanity-in-syria.
[545] See for instance BHRRC, "Danzer Group & SIFORCO lawsuits (re Dem. Rep. Congo)", available at: https://www.business-humanrights.org/en/danzer-group-siforco-lawsuits-re-dem-rep-congo.
[546] See for instance BHRRC, "Liberia: Dutch national faces eight year prison sentence for arms trading in Liberia", available at: https://www.business-humanrights.org/en/dutch-court-sentences-timber-trader-to-8-years-in-prison-for-providing-arms-to-liberia-in-violation-of-un-embargo#c25980.
[547] Marx et al above n 536.
[548] Trial International "Guus Kouwenhoven", last modified 12 July 2019, available at: https://trialinternational.org/latest-post/guus-van-kouwenhoven; Marx et al ibid.
[549] Jennifer Zerk, "Corporate liability for gross human rights abuses: Towards a fairer and more effective system of domestic law remedies", report prepared for the OHCHR, available at: https://www.ohchr.org/Documents/Issues/Business/DomesticLawRemedies/StudyDomesticLawRemedies.pdf.
[550] Axel Marx, Claire Bright, Nina Pineau and Jan Wouters, "Corporate Accountability Mechanisms in EU Member States for Human Rights Abuses in Third Countries", *European Yearbook on Human Rights* (forthcoming, 2019).
[551] *Yem Ban, Sophea Bun, Sem Kosal, Nol Nakry, Keo Ratha, Sok Sang and Phan Sophea v Doe Corporations, Phatthana Seafood Co., Ltd., Rubicon Resources, LLC, S.S. Frozen Food Co., Ltd. and Wales and Co. Universe Ltd.* No 2:16-cv-04271, (C.D. Cal, 15 June 2016).
[552] BHRRC, "Lidl lawsuit (re working conditions in Bangladesh)", available at: https://www.business-humanrights.org/en/lidl-lawsuit-re-working-conditions-in-bangladesh.
[553] BHRRC, "Auchan lawsuit (re garment factories in Bangladesh)", available at: https://www.business-humanrights.org/en/auchan-lawsuit-re-garment-factories-in-bangladesh.
[554] Carolijn Terwindt, Sheldon Leader, Anil Yilmaz-Vastardis and Jane Wright, "Supply Chain Liability: Pushing the Boundaries of the Common Law?" 8 *Journal of European Tort Law* (3) 261at 269.
[555] See Finland Country Report.
[556] See for instance the UK Country report discussion of complaints instituted by ClientEarth with the UK Financial Conduct Authority against several prominent insurers for failure to adequately disclose climate risk.
[557] ClientEarth, "World-first climate risk case launched over major coal plant in Poland", available at: https://www.clientearth.org/world-first-climate-risk-case-launched-over-major-coal-plant-in-poland/.

legally invalid on that basis.[558] Other early claims seek to hold individual defendant companies accountable for their contribution to climate change and its consequences.[559] For example, in the case of *Lliuya vs. RWE*, a Peruvian farmer sought compensation for damages from the German company RWE. The claim was based on the allegation that the defendant company, as a major emitter of greenhouse gases, contributed to the melting of two glaciers into a lake in his village of Huaraz, and the resulting risk of flooding. The claimant asked that the compensation should be based on the company's contributing share, proportional to its historic CO_2 emissions, in the cost of protecting the claimant's house and the village against such risk.[560] This is an area which is new and developing.[561]

These cases should be considered against the background of recent trends in climate change litigation against states,[562] aimed at pushing legislators and policy makers to adopt and implement climate change mitigation policies in accordance with the Paris Agreement.[563] For instance, the *Urgenda* case was based on the alleged inadequacy of the Dutch State's climate mitigation policy.[564] Upholding the judgment of the Hague District Court, the Court of Appeal of the Hague ruled that the Dutch State was acting unlawfully by failing to commit to a greater emission reduction which would allow to meet the standard deemed necessary by the latest climate science (i.e. a reduction of emissions by at least 25% by the end of 2020) to meet the 2°C target.[565] The Court grounded its ruling on the State's legal duty to ensure the protection of the life and family life of citizens, also in the long term, which is enshrined in the European Convention of Human Rights.[566] Another example is provided by the complaint submitted to the United Nations Human Rights Committee by ClientEarth, acting on behalf of a group of indigenous Australians from the Torres Strait region, against the Australian government on the basis of the alleged inaction of the Australian government, allegedly violating their human rights (by failing to protect their unique culture, and way of life, their environment and homelands).[567]

3.2.8 Due diligence in the Draft Treaty

On 26 June 2014, the UN Human Rights Council adopted a resolution establishing an open-ended intergovernmental working group (OEIGWG) on transnational corporations and other business enterprises with respect to human rights whose mandate was to "elaborate an international legally binding instrument to regulate, in international human rights law, the activities of transnational corporations and other business enterprises".[568]

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558 ClientEarth, "Court win in world-first climate risk case puts future of Ostrołęka C coal plant in question" (1 August 2019), available at: https://www.clientearth.org/press/court-win-world-first-climate-case-ostroleka-c-future-in-question.

559 See for example *Lliuya v RWE AG*, Case No. 2 O 285/15, Essen Regional Court, 15 December 2016; BHRRC, "RWE lawsuit (re climate change)", available at: https://www.business-humanrights.org/en/rwe-lawsuit-re-climate-change?utm_source=Corporate%20Legal%20Accountability%20Bulletin&utm_campaign=34f7f2275f-EMAIL_CAMPAIGN_2016_11_15&utm_medium=email&utm_term=0_7734b4f86e-34f7f2275f-&dateorder=dateasc. See also the NCP Final Statement in *ING* above n 443.

560 BHRRC ibid.

561 Chiara Macchi, "Climate Change, Business and Human Rights in the European Context: An Emerging Area of Legal Risk", draft paper presented at the conference Justice for Transnational Human Rights Violations At the Crossroads of Litigation, Policy and Scholarship, Bonavero Institute of Human Rights, Oxford, 19/20 June 2019, on file with the authors.

562 UN Environment Programme ("UNEP"), Columbia University and Sabin Center for Climate Change Law "The Status of Climate Change Litigation: A Global Review" (May 2017), available at : https://wedocs.unep.org/handle/20.500.11822/20767.

563 For instance, in *Urgenda Foundation v. Kingdom of the Netherlands,* a Dutch environmental group and 900 Dutch citizens successfully sued the newly elected Dutch government for revision of the GCG emissions reduction goals. *Urgenda Foundation v The State of the Netherlands (Ministry of Infrastructure and the Environment)*, Judgment of 24 June 2015.

564 *Urgenda* ibid.

565 The Hague Court of Appeal, *The State of The Netherlands v. Urgenda Foundation*, 9 October 2018, at para 76.

566 Ibid at para 45.

567 See also ClientEarth, "Human rights and climate change: World-first case to protect indigenous Australians", 12 May 2019, available at: https://www.clientearth.org/human-rights-and-climate-change-world-first-case-to-protect-indigenous-australians/.

568 UN Human Rights Council, "Elaboration of an International Legally Binding Instrument on Transnational Corporations and Other Business Enterprises with Respect to Human Rights", A/HRC Res. 26/9 (26 June 2014). On the Treaty, see in particular, John Ruggie, "Comments on the 'Zero Draft' Treaty on Business and Human Rights", *BHRRC*, available at: https://www.business-humanrights.org/en/comments-on-the-"zero-draft"-treaty-on-business-human-rights; Carlos Lopez, "Towards an International Convention on Business and Human Rights (Part I)", *Opinio Juris*, 23 July 2018, available at:

Following several sessions which took place between 2015 and 2017, the first official draft (the "Zero Draft") of the legally binding instrument on business and human rights was released on 16 July 2018[569] by Ecuador's Ambassador to the UN acting as Chair-Rapporteur of the OEIGWG.[570] On 16 July 2019, the OEIGWG published a Revised Draft of the business and human rights Treaty.[571]

The preamble of the Revised Draft expressly refers to the UNGPs. In particular, it provides that:[572]

> All business enterprises, regardless of their size, sector, operational context, ownership and structure have the responsibility to respect all human rights, including by avoiding causing or contributing to adverse human rights impacts through their own activities and addressing such impacts when they occur, as well as by preventing or mitigating adverse human rights impacts that are directly linked to their operations, products or services by their business relationships.

Article 3 of the Revised Draft defines its scope as applying "to all business activities, including particularly but not limited to those of a transnational character". This constitutes a change compared to the previous version (Zero Draft) which limited its scope of application to "business activities of transnational character",[573] and is in line with the position defended by the EU delegation during the negotiation.[574]

The concept of due diligence is contained in Article 5 of the Revised Draft Treaty under the heading "Prevention". It seeks to introduce mandatory due diligence through the adoption of legislation at the domestic level, establishing a legal duty for businesses to carry out due diligence.

The Revised Draft Treaty affirms, in Article 5.1 that:

> State Parties shall regulate effectively the activities of business enterprises within their territory or jurisdiction. For this purpose States shall ensure that their domestic legislation requires all persons conducting business activities, including those of a transnational character, in their territory or jurisdiction**,** to respect human rights and prevent human rights violations or abuses.

Article 5.2 specifies that:

> For the purpose of paragraph 1 of this Article, State Parties shall adopt measures necessary to ensure that all persons conducting business activities, including those of transnational character, to undertake human rights due diligence as follows:

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http://opiniojuris.org/2018/07/23/towards-an-international-convention-on-business-and-human-rights-part-i/; and Carlos Lopez, "Towards an International Convention on Business and Human Rights (Part II) ", *Opinio Juris*, 23 July 2018, available at: http://opiniojuris.org/2018/07/23/towards-an-international-convention-on-business-and-human-rights-part-ii/.

[569] UN Human Rights Council open-ended intergovernmental working group on transnational corporations and other business enterprises with respect to human rights ("OEIGWG"), "Legally Binding Instrument to Regulate, in International Human Rights Law, the Activities of Transnational Corporations and Other Business Enterprises, Zero Draft", 16 July 2018, available at: https://www.ohchr.org/Documents/HRBodies/HRCouncil/WGTransCorp/Session3/DraftLBI.pdf.

[570] Ibid.

[571] OEIGWG, "Legally Binding Instrument to Regulate, in International Human Rights Law, the Activities of Transnational Corporations and Other Business Enterprises", 16 July 2019, ("Revised Draft"), available at: https://www.ohchr.org/Documents/HRBodies/HRCouncil/WGTransCorp/OEIGWG_RevisedDraft_LBI.pdf.

[572] Ibid, Preamble.

[573] Zero Draft above n 569 at article 3.

[574] Nadia Bernaz, "Clearer, Stronger, Better? - Unpacking the 2019 Draft Business and Human Rights Treaty", *Rights as Usual*, 19 July 2019, available at: http://rightsasusual.com/?p=1339.

1. Identify and assess any actual or potential human rights violations or abuses that may arise from their own business activities, or from their contractual relationships;
2. Take appropriate actions to prevent human rights violations or abuses in the context of its business activities, including those under their contractual relationships;
3. Monitor the human rights impact of their business activities, including those under their contractual relationships;
4. Communicate to stakeholders and account for the policies and measures adopted to identify, assess, prevent and monitor any actual or potential human rights violations or abuses that may arise from their activities, or from those under their contractual relationships.

Whilst the wording used in the Zero Draft Treaty referred to "due diligence", the Revised Draft mirrors the terminology of the UNGPs by referring to "human rights due diligence".[575]

Article 4.5 of the Revised Draft provides that effective national procedures should be in place to ensure compliance with the legal obligation for businesses to carry out due diligence, "taking into consideration the potential impact on human rights resulting from the size, nature, context of and risk associated with the business activities, including those of transnational character", and that those procedures should be available to all natural and legal persons having a legitimate interest, in accordance with domestic law.

The revised draft also provides for a legal liability regime in case of harm caused to third parties by its "contractual relationships" resulting from a failure to prevent such harm through its due diligence processes when the company: [576]

> [S]ufficiently controls or supervises the relevant activity that caused the harm, or should foresee or should have foreseen risks of human rights violations or abuses in the conduct of business activities, including those of transnational character, regardless of where the activity takes place.

This limitation on "contractual relationships" has been strongly criticised as not in keeping with the UNGPs or the current regulation in this area.[577]

3.2.9 The usefulness and establishment of the concept of due diligence

As evidenced in the Market Practice sector, the concept of due diligence introduced by the UNGPs and expanded in the OECD Guidelines has become embedded in the discourse and practices of stakeholders across the spectrum. Stakeholders also strongly emphasise that the strength of these concepts should not be discarded for terminology that is more "vague".

These conclusions are also reflected in the literature. Andreas Rühmkorf and Lena Walker write about the terminology used to describe due diligence standards of care across various jurisdictions in the EU:[578]

> Due to national differences in legal systems and particularly due to the common

[575] Ibid.
[576] Revised Draft above n 571 at article 6.6
[577] For example, see Doug Cassel "Five ways the new draft treaty on business and human rights can be strengthened", *BHRRC*, 9 September 2019, available at: https://www.business-humanrights.org/en/five-ways-the-new-draft-treaty-on-business-and-human-rights-can-be-strengthened.
[578] Rühmkorf and Walker above n 371 at 4.

law / civil law divide, a number of different terms are used in the existing laws aimed at improving greater corporate accountability. These terms have different functions and meanings such as Sorgfaltspflicht in German law, duty of care in English law, due diligence (primarily also in English law) and vigilance in French law. They are all used in different contexts. Whilst the differences in terminology are due to the national context of legal systems, they hamper international discussions about how to impose greater corporate responsibility for global supply chains onto transnational corporations as there is no uniform term that is used. It appears as if common law lawyers and civil lawyers prefer using terminology and concepts that they are familiar with.

They further add:[579]

> [Due diligence] resonates with existing standards of duty of care in tort law and comparable concepts in civil law. It may be used to clarify these standards' application in the context of complex corporate structures and value chains.

The authors highlight that due diligence is a widely used and recognised concept at the international level. As a result, they advise against creating a new term or using a terminology that is specific to one system (such as *duty of vigilance*) as this would create confusion.[580] In addition, they explain that due diligence is more expansive than a duty of care in terms of enforcement as it is not limited to private action (a tort claim brought by alleged victims) but can also be subject to public enforcement (such as a fine for failure to conduct adequate due diligence).[581]

3.3 Environmental due diligence and climate change

3.3.1 Environmental due diligence

The due diligence developments following the introduction by the UNGPs and relevant to the mandate of this study, such as the French Duty of Vigilance Law and various other current proposals for mandatory due diligence at national level, refer to human rights and environmental harms. These developments are discussed at length elsewhere in this study. Similarly, environmental and human rights civil society organisations are jointly and separately advocating for mandatory due diligence at domestic and EU level. For example, in a recently published call to the European Commission, over 80 Human Rights and Environmental NGOs, together with trade unions called "for effective EU legislation that establishes a mandatory human rights and environmental due diligence framework for business, companies and financial institutions operating, or offering products or service, within the EU".[582]

However, separately from this framework, environmental laws have developed which, although not framed in due diligence language or a legal standard of care for companies, are nevertheless informative for the purposes of this study. In particular, the basic environmental principles of prevention and precaution have similarities with due diligence which may, in time, prove helpful for the interpretation of any regulatory measure. Moreover, various existing laws are aimed at the protection of the environment (see for example the table in Part IV Annexure C.3). An August 2019 study for the German Federal Ministry of Environment on the concept of environmental due diligence and how it could be applied as a legal requirement, indicates that corporate management systems which have been established for these laws on environmental

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[579] Ibid at 5.
[580] Ibid at 7.
[581] Ibid at 16.
[582] ECCJ above n 486

protection could "play an important role in the (partial) fulfilment of due diligence obligations".[583] For example, it states:[584]

> Environmental management systems previously focused primarily on direct environmental impacts (e.g. energy and material efficiency at specific sites). However, the most recent revision of the international environmental management standard ISO 14001 in 2015 and the amendment of the European Regulation for the Eco Management and Audit Scheme (EMAS) in 2017 and 2018 have strengthened aspects that are particularly relevant to the exercise of environmental and human rights due diligence. These include the increased consideration of indirect environmental impacts resulting from upstream and downstream stages of the value chain as well as of the views and expectations of relevant stakeholder groups, when determining the significant environmental impacts of an organisation.

The study states that "[i]n order to leverage these synergies, the environmental management system can be integrated into the company's greater due diligence processes".[585]

Interviewees in our study confirmed that, in the past, the human rights due diligence and environmental movements have developed in "silo[s]", but that they are beginning to recognise their commonalities, precisely because of the developments around mandatory due diligence regulation.

Indeed, across Europe the campaigns around mandatory due diligence legislation in Member States are driven by civil society consortia made up of human rights, corporate accountability and environmental organisations.

Similarly, environmental groups were some of the most proactive participants in our survey, in terms of reaching out to us, disseminating the survey amongst their networks, providing detailed and coordinated answers in optional text boxes, and asking to be further involved in the study. Many of these groups have been conducting their own internal studies and work on due diligence for impacts on the environment and people in agriculture, cocoa, forestry, timber, garment and other supply chains, and are actively exploring and pushing for due diligence regulation at domestic and EU level.[586]

Nicolas Bueno writes as follows to explain the link between environmental issues, including climate change impacts, and human rights:[587]

> Environmental issues are not specifically addressed in the UNGP, which cover only human rights. Corporations are nevertheless expected to respect and conduct due diligence with regard to all internationally recognized human rights, including those that necessarily entail environmental aspects, such as the rights to health, water, or food, or the rights of indigenous peoples. Additionally, Chapter VI of the OECD Guidelines defines the conduct that multinational enterprises should adopt to take due account of the need to protect the environment.

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[583] Cara-Sophie Scherf, Peter Gailhofer, Nele Kampffmeyer, Tobias Schleicher "Responsibility towards society and the environment: businesses and their due diligence obligations Background paper from the research project commissioned by the Federal Environment Agency", August 2019, German Federal Ministry for the Environment, Nature Conservation and Nuclear Safety, available at: https://www.umweltbundesamt.de/publikationen/umweltbezogene-menschenrechtliche at 7.
[584] Ibid.
[585] Ibid.
[586] For example, a recent report by Fern, Tropenbos International and Fairtrade, and authored by Duncan Brack, discusses mandatory due diligence within a range of options to achieve sustainable cocoa supply chains. Duncan Brack,"Towards sustainable cocoa supply chains: Regulatory options for the EU", report for Fern, Tropenbos International and Fairtrade, June 2019, available at: https://www.fern.org/news-resources/towards-sustainable-cocoa-supply-chains-regulatory-options-for-the-eu-1978/.
[587] Nicolas Bueno, "The Swiss Popular Initiative on Responsible Business: From Responsibility to Liability", in Liesbeth Enneking et al (eds.), A*ccountability, International Business Operations, and the Law*, London: Routledge (2020), 239.

Nevertheless, existing environmental laws are rarely phrased in terms of corporate due diligence requirements as a legal standard of care. Examples of existing environmental laws which require companies to take specific steps are discussed above. Moreover, existing soft law standards such as the EU Eco-Management and Audit Scheme[588] provide interesting examples of how due diligence requirements are applied, albeit currently on a voluntary basis.

As noted in the Market Practices section, an international and comparative environmental law expert, Ivano Alogna, who specializes in the legal models used for environmental regulation, noted that although there is currently a "bricolage" of legal instruments aimed at the protection of the environment, the French Duty of Vigilance Law is currently the "the first legislative model worldwide that places the burden of responsibility of prevention on the multinational company, which incurs its civil liability for its activities and environmental externalities...". He added that "this new legal model may offer a solid foundation to draft a European instrument of this kind".

There are nevertheless principles of international and national environmental laws which are worth mentioning as they are likely to be influential in the interpretation of any due diligence standard of care relating to the environment. Notably, the principles of prevention and the precautionary approach have similarities with the concept of due diligence insofar as they relate to pre-hoc decision making and risks management.

The principle of prevention is central to environmental protection laws. UNEP indicates that this is because:[589]

> In some instances it can be impossible to remedy environmental injury once it has occurred: the extinction of a species of fauna or flora, erosion, and the dumping of persistent pollutants into the sea create intractable, even irreversible situations. Even when harm is remediable, the cost of rehabilitation is often very high. In many instances it is impossible to prevent all risk of harm. In such instances, it may be judged that measures should be taken to make the risk "as small as practically possible" in order to allow necessary activities to proceed while protecting the environment and the rights of others.

The prevention of irremediable harms is also a core concept in the UNGPs. Guiding Principle 24 provides:

> Where it is necessary to prioritize actions to address actual and potential adverse human rights impacts, business enterprises should first seek to prevent and mitigate those that are most severe or where delayed response would make them irremediable.

In describing an understanding of risk management process that is reminiscent of the due diligence concept, UNEP described the prevention principle as:

> [A]n overarching aim that gives rise to a multitude of legal mechanisms, including prior assessment of environmental harm, and licensing or authorizations that set out the conditions for operation and the remedial consequences for violation of the conditions. Emission limits and other product or process standards, the use of best available techniques (BAT), and other similar techniques can all be seen as applications of prevention.

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588 Above n 485.
589 Dinah Shelton and Alexandre Charles Kiss, "Chapter 2: Basic Principles of Environmental Protection" in *Judicial Handbook on Environmental Law*, United Nations Environment Programme ("UNEP"), 2005, at 20, referring to *Solothurn v. Aargau*, Switzerland Bundesgericht (Federal Tribunal), 1 Nov. 2000.

> Prevention is also linked to the notion of deterrence and the idea that disincentives such as penalties and civil liability will cause actors to take greater care in their behaviour to avoid the increased costs, thus preventing pollution from occurring.

It is clear that although the concept of corporate due diligence is not utilised, the idea of incentivising management process to prevent or minimise risks, which may otherwise be irremediable, through penalties and civil liability which cause actors to "take greater care in their behaviour", is central to this study.[590]

The precautionary principle is similarly relevant. Principle 15 of the Rio Declaration on Environment and Development (1992)[591] describes the precautionary approach as follows:

> In order to protect the environment, the precautionary approach shall be widely applied by States according to their capabilities. Where there are threats of serious or irreversible damage, lack of full scientific certainty shall not be used as a reason for postponing cost effective measures to prevent environmental degradation.

UNEP indicates that:[592]

> While there is no single agreed formulation or "principle" of precaution that is used in all contexts, and precaution has not acquired generally accepted status as a legal principle in its own right or as customary international law, there is a basic concept of precaution that animates much of modern environmental protection regimes - the notion that environmental regulators often have to act on the frontiers of knowledge and in the absence of full scientific certainty. Precaution has variously been associated with the ideas that: 1) scientific uncertainty should not be used as a reason not to take action with respect to a particular environmental concern; 2) action should a*ffirmatively* be taken with respect to a particular environmental concern; 3) those engaging in a potentially damaging activity should have the burden of establishing the absence of environmental harm; and 4) a State may restrict imports based on a standard involving less than full scientific certainty of environmental harm. [Original emphasis]

Again, a notable similarity with the concept of due diligence is that "those engaging in the potentially damaging activity should have the burden of establishing the absence of the environmental harm". Moreover, the idea that an actor should act with precaution for potential risks, even if it is not entirely certain that those risks will occur, aligns with the enquiry regarding prioritisation of severe risks based on an impact assessment as described in the UNGPs.

The German country report for this study highlights examples of how the precautionary principle is translated into due diligence at national level through laws for the protection of the environment. German country reporter Daniel Augenstein writes:

> Many due diligence obligations in German environmental law owe their existence to the precautionary principle which, as laid down in Article 20a of the German

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[590] Shelton and Kiss ibid at 21 lists further examples of cases which discuss the principle of prevention: *Greenpeace Australia Ltd. v. Redbank Power Company Pty. Ltd. and Singleton Council* 86 LGERA 143 (1994 Australia); *Leatch v. National Parks and Wildlife Service and Shoalhaven City Council* 81 LGERA 270 (1993, Australia); *Vellore Citizens Welfare Forum v. Union of India AIR* 1996 SC 2715; *Shela Zia v. WAPDA* Vol. XLVI All Pakistan Legal Decisions 693.
[591] Rio Declaration of Environment and Development (1992), available at: http://www.unesco.org/education/pdf/RIO_E.PDF (last accessed 5 September 2019).
[592] Shelton and Kiss above n 589.

> Constitution, requires the state to prevent risks to the environment from materialising even where cause-and-effect relationships are not fully established scientifically. The federal law that provides for protection of humans, animals and the environment against harmful emissions (Bundesimmissionsschutzgesetz, BISchG) is one such example.

The German country report further states that in terms of this law:

> The duty of precaution (§ 5 I (1) No 2) requires operators to take measures, in accordance with the scientific and technical state of the art ('Stand der Technik', § 3 VI (1) BISchG), to reduce risks of environmental nuisance whose materialisation is possible yet not sufficiently probable to trigger a duty of protection. The concrete scope of the latter duty is determined in the light of criteria such as the risk-potential of the emissions, the severity of damages to be expected, and the economic costs of minimising risks.

Again, the similarities with due diligence as described in the UNGPs is noted regarding the assessment and prioritisation of severe risks, relevant to the context.

The German country report further highlights two important features of this law, which is common for laws aimed at the protection of the environment:

> Compliance of operators is *monitored and enforced* by the competent public authority. Unlike the duty of protection, the duty of precaution is generally not considered to confer subjective rights on third parties.

Although the precautionary principle does not itself give rise to a legal duty for companies at international level, it has been used to interpret existing duties in case law. For example, in the case of *Asociacion Coordinadora de Usuarios, Consumidores y Contribuyentes v Enre-Edesur*,[593] an Argentinian court referred to the principle of precaution in making an order which required a company to produce a report, through stakeholder engagement, on the potential negative impacts of an electricity grid, and how they will be prevented or mitigated. The court temporarily suspended operations until the report was produced.

3.3.2 Due diligence and climate change

Given the key focus on climate change due diligence within the mandate of this study, it is worth discussing in more depth the recent developments relating to due diligence for companies' climate change impacts. Many of these developments took place as this study was being undertaken.

In 2018, the Expert Group on Climate Obligations of Enterprises released the Principles on Climate Obligations of Enterprises which "aim to provide a legal basis for active investment management and engagement geared at stimulating enterprises to comply with their legal obligations" to reduce their greenhouse gases emissions.[594]

On 25 June 2019, a report from the UN Special Rapporteur on extreme poverty and human rights reaffirmed the impact of climate change on human rights in no uncertain terms. The report criticises states and other actors for "giving only marginal attention to human rights in the conversation on climate change"[595] for decades, and that "as a full-

[593] *Asociacion Coordinadora de Usuarios, Consumidores y Contribuyentes v. ENRE-EDESUR*, Federal Appellate Tribunal of La Plata (2003). See Shelton and Kiss ibid at 21-22.
[594] Expert Group on Climate Obligations of Enterprises, *5 Principles on Climate Obligations of Enterprises*, Eleven International Publishing, Den Haag (2018), available at: https://climateprinciplesforenterprises.files.wordpress.com/2017/12/enterprisesprincipleswebpdf.pdf.
[595] Report of the Special Rapporteur on extreme poverty and human rights, "Climate change and poverty", A/HRC/41/39 (July 2019), available at: https://documents-dds-ny.un.org/doc/UNDOC/GEN/G19/218/66/PDF/G1921866.pdf?OpenElement at 1.

blown crisis bears down on the world, business as usual is a response that invites disaster".[596] It emphasises the role to be played by companies, alongside other actors, in providing and implementing solutions to climate change,[597] through "a radically more robust, detailed, and coordinated approach".[598]

In addition, in a September 2019 statement, UN High Commissioner for Human Rights, Michelle Bachelet, stated that climate change is "the greatest ever threat to human rights".[599] It is now an established principle that "adopt[ing] legal and institutional frameworks that protect" against harm resulting from human-made climate change is both part of the state duty "to protect against environmental harm that interferes with the enjoyment of human rights, including harm caused by private actors",[600] and of the corporate responsibility to respect human rights set out in the UNGPs.[601] It is now widely accepted that "climate change poses an immediate and far-reaching threat to people and communities around the world and has implications for the full enjoyment of human rights".[602]

Also in September 2019, during Climate Week, the UN Global Compact reported during that 87 companies committed to climate targets across their operations and value chains, with a view to limiting temperature rise to 1.5C above pre-industrial levels.[603]

In 2014, the International Bar Association Task Force on Climate Change Justice and Human Rights published its landmark report on Achieving Justice and Human Rights in an Era of Climate Disruption.[604] The Report recommends a "multifaceted" approach to corporate responsibility which include, *inter alia*:

> As a first step, corporations should adopt and promote the UN Guiding Principles on Business and Human Rights as they pertain to human rights and climate change.

The report further explains that:

> To advance corporate responsibility specifically in the context of climate change, a model policy should commit the corporation to take a number of concrete steps. Such measures must include due diligence of corporate projects, including the environmental practices of the company's affiliates, and as far as reasonably practicable, its major contractors and suppliers as well as compliance with reporting obligations [...]. Secondly, the corporation should implement a due-diligence process to identify, prevent, mitigate and account for its actual climate change impacts. While awareness is the first step, the corporation must translate its awareness into active efforts to minimise or reverse the impacts of its actions on climate change and human rights. The corporation should consider measures it can implement to assist in achieving the objective of limiting global warming to no more than a 2°C increase. The corporation's goal should be to implement the most advanced available technology to minimise its carbon footprint. In situations

596 Ibid at 3.
597 Ibid.
598 Ibid at 1.
599 Agence France-Presse, "Climate crisis is greatest ever threat to human rights, UN warns", The Guardian (9 September 2019), available at: https://www.theguardian.com/law/2019/sep/09/climate-crisis-human-rights-un-michelle-bachelet-united-nations.
600 Report of the Independent Expert on the issue of human rights obligations relating to the enjoyment of a safe, clean, healthy and sustainable environment, John H. Knox, A/HRC/25/53 (30 December 2013) at 1.
601 Macchi above n 561 at 1.
602 UN Human Rights Council Resolution 7/23, "Human rights and climate change" (28 March 2008), available at : https://ap.ohchr.org/documents/E/HRC/resolutions/A_HRC_RES_7_23.pdf.
603 United Nations Global Compact, the Science Based Targets initiative (SBTi) and the We Mean Business coalition "87 major companies lead the way towards a 1.5°C future at UN Climate Action Summit", *UN Global Compact* (22 September 2019), available at: https://www.unglobalcompact.org/news/4476-09-21-2019.
604 International Bar Association Climate Change Justice and Human Rights Task Force Report, "Achieving Justice and Human Rights in an Era of Climate Disruption", July 2014.

where negative impact on the environment is unavoidable given current technology or if the cost of such technology is prohibitive, the corporation bears responsibility for corresponding mitigation and remediation. Thirdly, the corporation should implement remediation processes that allow for open communication with stakeholders most affected by the corporation's operations. [...]

The OECD Guidelines set out that companies are expected to carry out due diligence in respect to their environmental impacts, including climate impacts. Moreover, the UNGPs, read with the OECD Guidance on Responsible Business Conduct, the Paris Agreement, and recent legislation such as the French Duty of Vigilance Law and the EU non-financial reporting directive, all confirm the trend observed by interviewees that climate change impacts are to be viewed as included within due diligence insofar as they relate to the impacts of the individual company (and the steps it can take to address them) on people and the planet.

The evidence from our surveys and interviews shows that the language of "climate change due diligence" is currently very rarely used, indicating that self-standing due diligence processes which focus exclusively on climate change are rare. Interviewees also indicated that whereas their companies do consider their climate change impacts, this is usually situated in other departments. However, overall, stakeholders across business and other groups agreed that environmental, climate change and other sustainability impacts are understood to be within scope of a company's existing due diligence requirements. Business survey respondents indicated that environmental impacts, including air pollution, greenhouse emissions and climate change aspects, are frequently viewed as included in their due diligence processes, either expressly or implied.

These findings should be viewed within the context of the ongoing evolution of due diligence requirements, and steps to implement these within corporate practice, which are still relatively new. In particular, the OECD Guidelines expect companies to carry out due diligence in respect to their environmental impacts, including climate impacts. The French Duty of Vigilance Law and the EU non-financial reporting directive confirm the trend observed by interviewees that climate change impacts are to be viewed as included within due diligence. However, the OECD Guidance on Responsible Business Conduct was adopted on 31 May 2018,[605] and the EU Non-Financial Reporting Directive required annual reporting from 2018 onwards.[606]

These laws have not yet generated any case law to clarify the application of these obligations, in particular with respect to how climate change is included as part of due diligence expectations. As such, they have also had a very short opportunity to inform corporate practices. Indeed, during the course of this study, the EU published its non-binding guidance on reporting climate-related information,[607] discussed above. A few weeks prior, as discussed below, the Netherlands OECD NCP clarified concrete ways in which companies' individual due diligence actions can include targets to address climate change, even in the absence of agreed international measures and standards.[608] In determining the company's due diligence responsibilities, reference was made to the relevant company's steps in terms of the Paris Agreement on Climate Change.[609]

[605] OECD RBC Guidance above n 370.
[606] EU Non-Financial Reporting Directive above n 24.
[607] EU Guidelines on non-financial reporting: Supplement on reporting climate-related information, C/2019/4490 of June 2019. See also European Commission, "Sustainable finance: Commission publishes guidelines to improve how firms report climate-related information and welcomes three new important reports on climate finance by leading experts", 18 June 2019, available at: http://europa.eu/rapid/press-release_IP-19-3034_en.htm.
[608] NCP Final Statement in ING above n .
[609] See Paris Agreement on Climate Change, available at: https://unfccc.int/process-and-meetings/the-paris-agreement/d2hhdC1pcy, (last accessed 19 June 2019).

Similarly, as can be seen in the regulatory review of this study, regulatory developments requiring due diligence, such as the French Duty of Vigilance Law and the proposed Swiss law on mandatory due diligence, expressly require due diligence for human rights *and* environmental impacts. Again, these requirements are either new or still in proposed form. The few existing examples of climate change litigation are similarly very recent, and insofar as they related to *state* due diligence obligations relating to climate change,[610] were not framed relating to *corporate* due diligence. As a result, to date, courts are yet to clarify specific climate change due diligence obligations for individual companies.

These developments, along with other developments in the field of climate change law and policy at the EU level, have led authors to argue that "any coherent human rights due diligence regulation that may emerge in the near future at the EU level should necessarily include the climate change responsibilities of corporations".[611] It is noted that the EU Action Plan on Sustainable Finance, in addition to calling for an assessment of due diligence which forms the mandate of this study, also calls for an assessment of "measurable sustainability targets".[612]

The time will tell how courts will apply these mandatory due diligence requirements with respect to human rights and environmental impacts, and in turn, how this will influence corporate practice. The status quo is constantly developing as new regulations are adopted and proposed at domestic level. It is likely that any regulatory mechanisms at domestic and, potentially, EU level which follow the trend to expressly include environmental impacts as part of mandatory due diligence may lead to a change in corporate practices also with respect to express inclusion of climate change impacts.

An important clue as to how due diligence expectations for climate change impacts may be applied in any future litigation is provided by the OECD NCP statement in the matter of *Oxfam Novib, Greenpeace Netherlands, BankTrack and Friends of the Earth Netherlands (Milieudefensie) v ING*.[613] The complaint related to the bank's alleged failures to set measurable objectives and targets relating to the climate impacts of its finance activities. In its final statement, the NCP found with regard to companies' responsibility to measure how they meet targets:[614]

> The NCP stresses that absence of a methodology or international accepted standard will not dismiss companies, including financial institutions, to seek measurement and disclosure of environmental impact "in areas where reporting standards are still evolving such as, for example, social, environmental and risk reporting. This is particularly the case with greenhouse gas emissions". At the same time, the NCP takes into consideration that financed emissions are indirect and thus more difficult to measure and control. Meanwhile it has to be noted ING made an effort to design a standard.

The NCP further finds with respect to the setting of targets:[615]

> As such, the NCP observes that the OECD Guidelines demand that ING, and other commercial banks, put effort into defining, where appropriate, concrete targets to manage its impact towards alignment with relevant national policies and international environmental commitments. Regarding climate change, the Paris

[610] BHRRC, "Turning up the heat: Corporate legal accountability for climate change", *Corporate Legal Accountability Annual Briefing 2018*, available at: https://www.business-humanrights.org/sites/default/files/English_ES_FINAL.pdf at 1.
[611] Macchi above n 561 at 3.
[612] Action 10 of the Communication from the Commission to the European Parliament, the European Council, the Council, the European Central Bank, the European Economic and Social Committee and the Committee of the Regions Action Plan: Financing Sustainable Growth, COM/2018/097 final, 8 March 2018, available at: https://ec.europa.eu/info/publications/180308-action-plan-sustainable-growth_en.
[613] NCP Final Statement in *ING* above n 443.
[614] Ibid at 5.
[615] Ibid at 5.

> Agreement is currently the most relevant international agreement between states, a landmark for climate change, signed by the State of the Netherlands.
>
> The NCP is sensitive to the argument that financed emissions are indirect and thus more difficult to measure and control. The NCP considers that impact measurement of financed emissions is a new field of expertise, and recognizes the fact that ING, and banks like ING, face considerable challenges in developing an appropriate methodology, including the setting of intermediate targets.
>
> As the Guidelines ask for periodically reviewing the relevance of objectives or targets, and given the long term objectives of the climate debate, the NCP encourages ING to set intermediate targets as well.

These findings of the NCP are particularly relevant to this study in two important respects. Firstly, it clarifies that even where there is no agreed methodology for measuring targets (such as in the area of climate change and other environmental harms), this does not excuse companies from the responsibility to set measurable targets for the purposes of environmental due diligence in accordance with the OECD Guidelines. The NCP refers to the Paris Agreement on climate change as providing some indication of how to link individual companies' due diligence and their climate change targets.

Secondly, in the company's defence, it raised the fact that it had already, in May 2015, committed to "a future methodology to be developed by the Science Based Target Initiative".[616] These existing commitments and steps taken were noted and taken into account by the NCP in its findings. This illustrates the point below regarding due diligence as a defence, and particularly the desirability for companies of having robust processes in place, which can be pointed towards should an issue arise.

Whereas until recently it was not clear how an individual company could be held (legally) liable to carry out due diligence for large-scale impacts such as climate change, the above case illustrates that due diligence obligations are now increasingly being understood as including climate change due diligence. In threatening legal action if Total does not correct its vigilance plan (i.e. its due diligence steps) under the French Duty of Vigilance Law, the consortium of local city councils and civil society organisations state:

> The global effort must be shared by all. Through this first public interpellation, local communities and NGOs send a clear message to the whole economical world: the climate burden must be tackled by all.

In September 2019, forest fires in the Amazon spurred investors to coordinate, through the UN Principles for Responsible Investment (PRI), a statement which calls on investee companies to take measurable action for their deforestation and resulting climate change impacts.[617] The statement declares that:

> As investors, we see deforestation and the associated impacts on biodiversity and climate change as systemic risks to our portfolios and see the reduction of deforestation as a key solution to managing these risks and contributing to efficient and sustainable financial markets in the longer term.

In the statement, investors call on companies to:

> [R]edouble their efforts and demonstrate clear commitment to eliminating deforestation within their operations and supply chains, including by:

[616] Ibid at 2.
[617] UN PRI, "Investor statement on deforestation and forest fires in the Amazon", (September 2019), available at: https://d8g8t13e9vf2o.cloudfront.net/Uploads/g/i/u/investorstatementondeforestationandforestfiresintheamazon_76915.pdf.

1. Publicly disclosing and implementing a commodity-specific no deforestation policy with quantifiable, time-bound commitments covering the entire supply chain and sourcing geographies.
2. Assessing operations and supply chains for deforestation risk and reduce this risk to the lowest possible level, disclosing this information to the public.
3. Establishing a transparent monitoring and verification system for supplier compliance with the company's no deforestation policy.
4. Reporting annually on deforestation risk exposure and management, including progress towards the company's no deforestation policy.

These steps closely follow the components and language of due diligence: assessment, monitoring, reporting, as well as the implementation of policies covering the entire supply chain. Moreover, by referring to "quantifiable, time-bound commitments", the statement forms part of an increasing trend whereby companies are required to take measurable steps towards their climate change impacts, even in the absence of internationally agreed corporate targets, as also envisioned in the OECD Guidelines and the NCP statement in the matter of *ING.*

As further confirmation of this trend, the proposed EU Regulation on disclosures relating to sustainable investments and sustainability risks specifically requires information relating to "adherence to responsible business conduct codes and internationally recognised standards for due diligence and reporting and, where relevant, the degree of alignment with the long-term global warming targets of the Paris Climate Agreement".[618]

It is within this context that this study discusses a regulatory sub-option which, in addition to a general duty, would establish particular requirements for large companies in relation to due diligence for their climate change impacts.

3.4 Due Diligence, sustainability and the SDGs

Insofar as this study is mandated within the context of sustainable finance, it is important to consider how due diligence fits in with sustainability more broadly.

A number of SDGs are particularly relevant to the study:

- SDG 8 on Decent Work;
- SDG 12 targeting Responsible production and consumption, in particular with regard to the following SDG Targets:
    - 12.4 By 2020, achieve the environmentally sound management of chemicals and all wastes throughout their life cycle, in accordance with agreed international frameworks, and significantly reduce their release to air, water and soil in order to minimize their adverse impacts on human health and the environment;
    - 12.6 Encourage companies, especially large and transnational companies, to adopt sustainable practices and to integrate sustainability information into their reporting cycle;
    - 12.a Support developing countries to strengthen their scientific and technological capacity to move towards more sustainable patterns of consumption and production;

[618] Article 3gamma of the EU proposal above n 471.

- SDG 16 on peace, justice and strong institutions.

It has been established by the UN, which is responsible for the SDGs agenda as well as the interrelated business and human rights framework, that undertaking appropriate human rights and environmental due diligence contributes to sustainable development. In its 2018 Report, the UN Working group on the issue of human rights and transnational corporations and other business enterprises explained that:[619]

> Business strategies to contribute to the Sustainable Development Goals are no substitute for human rights due diligence. On the contrary, robust human rights due diligence enables and contributes to sustainable development. For businesses, the most powerful contribution to sustainable development is to embed respect for human rights in their activities and across their value chains, addressing harm done to people and focusing on the potential and actual impacts — as opposed to starting at the other end, where there are the greatest opportunities for positive contribution. In other words, businesses need to realize and accept that not having negative impacts is a minimum expectation and a positive contribution to the Goals.

3.5 Due Diligence and corruption

Country reporters were asked to discuss due diligence requirements as they relate to corruption. As is evidenced from the country reports, corruption is commonly regulated at Member State level in terms of criminal law, and do not ordinarily provide remedies for victims. Moreover, the framework on which this study is based, including the evolution of the concept of due diligence from the UNGPs to the OECD Guidelines and the French Duty of Vigilance Law as set out in the European Parliament report, frame due diligence in terms of human rights and environmental harms, which are currently unregulated by corruption regulation. As such, corruption due diligence falls outside of the focus of this study for the purposes of "human rights and environmental" due diligence.

However, the regulation of bribery and corruption law provide interesting comparators for this study, insofar as corruption regulation require similar group-wide, and often transnational, risk management procedures. The UK Bribery Act, for example, provides for a due diligence defence similar to the one under consideration in this study.[620] In this respect, it is likely that companies' experience with due diligence practices for bribery laws have also informed their responses to the possible impacts of the regulatory options for this study.

Moreover, a study cited elsewhere in this report by Genevieve LeBaron and Andreas Rühmkorf compared the practices of companies in response to the UK Bribery Act (which includes state-based oversight and sanctions for enforcement such as considered in our Option 4.3(b) and the UK Modern Slavery Act (a reporting requirement similar to our Option 3). They find that the state-based enforcement model, which in the case of the UK Bribery Act is also tied to criminal liability, drives significantly more implementation in corporate practice than reporting requirements without sanctions.[621]

The Assessment of Options section furthermore relies on information available from assessments of corruption due diligence requirements, including relating to possible fines and impacts on the costs for public authorities of state-based enforcement mechanisms.

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[619] UN Working Group above n 376 at para 10.
[620] Section 7 of the UK Bribery Act 2010.
[621] Genevieve LeBaron and Andreas Rühmkorf, "Steering CSR Through Home State Regulation: A Comparison of the Impact of the UK Bribery Act and Modern Slavery Act on Global Supply Chain Governance", *Global Policy* Vol 8 Supp. 3 (May 2017) 15-28 at 26.

3.6 Due Diligence in the agricultural sector, including coffee, tea and cocoa subsectors

Generally speaking, stakeholders have expressed their views against regulatory measures which would be limited to a specific sector or commodity as they would contribute to increasing the fragmentation of due diligence requirements across sectors and commodities, creating further legal uncertainty. However, in the implementation of any overarching EU level regulations on mandatory due diligence for adverse human rights and environmental impacts in companies' operations and in their supply chains, considerations will need to be given to the specificity of such sectors.

In this context, the TOR refers to the examples of the agricultural subsectors of coffee, tea and cocoa. As a result, survey respondents were specifically asked about their involvement in these subsectors, the findings of which are set out in the Market Practices sector. Given the general mandate of this study, and the samples, it is not relevant to provide detailed findings in accordance with specific subsectors.

The literature analysed similarly sets out the position in relation to these subsectors as they are relevant to due diligence developments. The cocoa subsector in particular has been linked by various studies and stakeholders (see the Market Practices section) to issues of child labour and deforestation.[622] For example, a recent report of Fern Tropenbos International and Fairtrade[623] which is discussed in further detail throughout this study, notes the widespread issues prevalent in the cocoa sector and the limitations of voluntary initiatives "such as certification schemes and company programmes" to "tackle these problems":

> There is increasing acknowledgement, however, that while these current initiatives have had some positive impacts, they have not succeeded, and are not likely to succeed, in tackling low prices and poverty, child labour, deforestation and illegality across the whole cocoa sector.

The report calls for an intervention at the EU level:

> Since the EU is the world's largest importer of cocoa and cocoa products, EU consumption, and any standards it imposes on imports, has the potential to affect the conditions of production in the countries of origin. There is, accordingly, a strong case that EU-wide government action or regulation should be considered, but as yet there is no consensus on what it might be.

In applying to concept of due diligence to these subsectors it should be taken into consideration that they mainly rely on smallholders.[624] This could be done in non-binding guidance accompanying any general regulation, as discussed further in the Problem Analysis and Regulatory Options section.[625]

3.7 Due Diligence for child labour

Survey respondents expressed their views against regulatory measure which focuses on one specific issue, such as child labour or modern slavery (which were the specific

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[622] Mighty Earth, authored by Etelle Higonnet, Marisa Bellantonio and Glenn Hurowitz, "Chocolate's Dark Secret: How the Cocoa Industry Destroys National Parks" (August 2019), available at: http://www.mightyearth.org/reports/.
[623] Brack above n 586.
[624] Ibid at 50.
[625] Ibid.

examples provided in the survey).[626] Instead, the majority of survey respondents across the spectrum agreed that regulation should cover all human rights and environmental impacts. Interviewees and survey respondents in optional text boxes similarly noted that issue-specific regulation creates further fragmentation and risk detracting attention from other adverse human rights impacts, by incentivising companies to prioritize efforts to address a particular issue to the detriment of other potentially more salient human rights issues in the supply chain of a particular company.[627] These findings are discussed and analysed in the Market Practices and Problem Analysis and Regulatory Options sections respectively.

As a result, and given the mandate of the study referring to a general due diligence framework, an issue-specific sub-option was not included within the regulatory options. Nevertheless, insofar as the TOR expressly refers to child labour, the definition of human rights provided to survey participants expressly referred to child labour. The impacts on child labour were also included in the detailed questions about possible regulatory impacts posted to survey respondents. Interviewees included experts at international organisations and NGOs which specialize in due diligence for child labour. In addition, an analysis of issue-specific regulation is covered in the Market Practices, the Regulatory Review, the Country Reports, the Problem Analysis and Regulatory Options and the Assessment of Options.

In particular, the example of the 2019 Dutch Child Labour Due Diligence Law, which was adopted during the course of this study, is discussed throughout the study, and in particular detail in the Netherlands Country report.

4. Domestic frameworks

4.1 Country reports: Twelve selected EU Member States

At domestic level, due diligence requirements have been developed and applied in various ways. This section reviews the relevant laws and standards requiring due diligence for human rights and environmental impacts in twelve EU Member States, namely Belgium, Denmark, Finland, France, Germany, Ireland, Italy, the Netherlands, Poland, Spain, and Sweden, and the UK.

The country reports were authored by country expert reporters with expertise in the relevant domestic legal system. For ease and clarity, the country reports will follow below as standalone sections, like chapters in a book. The authors of each country report are named under each respective country heading.

The country reports are preceded by an overview of their findings, authored by Professor Robert McCorquodale for BIICL.

4.2 Other domestic developments

This section briefly considers some relevant developments in countries outside of the EU.

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[626] The majority (47.06%) of business respondents preferred regulation to apply across all issues. Less than half of this number (23.53%) preferred regulation which focuses only on one issue such as modern slavery or child labour. Only 4.9% (the least selected option, below no preference), preferred "[i]ssue-specific regulation covering another specific human rights or environmental issue". Similarly, general respondents expressed a very strong preference (74.15%) for "[r]egulation which covers all EU-recognised human rights and environmental impacts." Only 9.52% expressed a preference for issue-specific regulation "for example covering only issues of child labour or modern slavery". The least selected option by only 2.04% of general survey respondents was "[i]ssue-specific regulation covering another specific human rights or environmental issue".
[627] See discussions in Section IV Problem Analysis and Regulatory Options.

4.2.1 Switzerland

In Switzerland, the Popular Initiative on Responsible Business was launched by the Swiss Coalition for Corporate Justice after having collected the requisite threshold of 100,000 signatures from Swiss citizens.[628]

The Swiss Responsible Business Initiative seeks to impose direct human rights and environmental obligations on Swiss-based companies and introduce mandatory due diligence across all sectors through a revision of the Swiss Constitution. In particular, it proposes to add an article 101a entitled "Responsibility of Business" to the Swiss Constitution empowering the Swiss government to take legislative measures in order to regulate the obligations of Swiss-based companies with regard to human rights and the environment. Paragraph 2.a of Article 101a of the Initiative states:[629]

> [C]ompanies must respect internationally recognized human rights and international environmental standards, also abroad; they must ensure that human rights and environmental standards are also respected by companies under their control.

Paragraph 2.b of Article 101a requires Swiss-based companies to carry out "appropriate due diligence" so as to:[630]

> [I]dentify real and potential impacts on internationally recognized human rights and the environment; take appropriate measures to prevent the violation of internationally recognized human rights and international environmental standards, cease existing violations, and account for the actions taken.

The due diligence requirements under the Swiss Initiative apply to "controlled companies as well as to all business relationships". In Swiss Law, "controlled companies" usually refer to subsidiaries of parent companies. However, the concept can also encompass other entities over which the company exercise economic control, such as the supplier of a Swiss company which is its only purchaser.[631] The concept of "controlled companies", which is not a concept familiar to UNGPs terminology, is narrower than the UNGPs's reference to "leverage".[632]

In terms of scope, the Responsible Business Initiative covers all the companies that have their registered office, central administration or principal place of business in Switzerland. The text of the draft acknowledges that the needs of small and medium-sized companies that have limited risks of this kind are to be taken into account.[633]

Paragraph 2.c of the text provides for a specific liability regime of Swiss companies for the extraterritorial damages "caused by the companies under their control" where these companies have "in the course of business, committed violations of internationally recognized human rights or international environmental standards". This regime has been modelled on the existing Swiss provision concerning principal or vicarious liability.[634] The text of the initiative provides that the controlling companies are not liable if they can prove that they carried out their due diligence obligations appropriately. In that respect, it provides for a reversal of the burden of proof which addresses some of

[628] Bueno above n 587 at 12.
[629] SCCJ "Initiative Text" above n 493 at para 1.a.
[630] Ibid.
[631] Ibid at para 1.
[632] UNGP 19.
[633] Ibid at para 1.b.
[634] Ibid at para 2.

the hurdles encountered by claimants in bringing evidence concerning the conduct of controlled companies located abroad.[635]

On 14 June 2018, the National Council adopted a counter-proposal of the text, which is less ambitious than the original text of the Swiss Responsible Business Initiative.[636] In particular, the counter-proposal is narrower in terms of scope as it applies to companies exceeding two of the three following thresholds: a balance sheet total of 40 million CHF/USD; a turnover of 80 million CHF/USD; or 500 full-time employees.[637] It also applies to SMEs with particular high risk activities. In addition, the liability regime is limited to parent companies for the damage caused by effectively controlled subsidiaries.[638] It is also limited to damage to life and limb or property that are the result of a violation of international standards which have been ratified by Switzerland.[639]

Nicolas Bueno writes about the Swiss National Council legislative proposal:[640]

> After setting the general goal of the initiative in Paragraph 1, the initiative text entails three elements to implement this goal in Paragraph 2. First, Article 101a(2)(b) introduces and defines the scope of a mandatory due diligence provision in the Swiss Constitution. Article 101a(2)(c) then addresses the liability of companies based in Switzerland, including their liability for harm caused by companies under their control. Finally, Article 101a(2)(d) aims to ensure that the introduced mandatory due diligence and liability provisions will apply even though the human rights or environmental-related harm typically occurs abroad.

Bueno further adds:[641]

> Concretely, the introduction of a mandatory due diligence provision objectifies the expected conduct that Switzerland-based companies must apply with a view to preventing adverse human rights and environmental impacts in Switzerland and abroad. In this regard, the text of the initiative does not distinguish between the three scenarios presented above: causing an adverse impact, contributing to an adverse impact through the enterprise's own activities, and adverse impacts directly linked to the enterprise's operations by a business relationship. It broadly states that due diligence 'duties apply to controlled companies as well as to all business relationships'. However, according to the explanation of the initiative text, section (2)(b) introduces a mandatory due diligence provision based on the UNGPs and the OECD Guidelines for Multinational Enterprises. Therefore, the international framework may provide guidance on how to interpret the text of the initiative. Although not expressly referenced in the text, this standard of conduct should also help to identify whether a company has committed a fault and should be held liable *for its own actions and omissions* on the basis of the general tort of negligence.

On 18 December 2019, the Council of States adopted another proposal in which the due diligence requirements would be restricted to the conflict minerals sector and to enterprises providing goods and services in Switerland for which there is a reasonable suspicion that they have been supplied or produced using child labour. This proposal also no longer contains the civil liability mechanism. The two chambers of the Swiss Parliament will discuss these two parliamentary proposals in first half of 2020, and,

[635] Ibid.
[636] SCCJ, "How does the parliamentary counter-proposal differ…?" above n 493.
[637] Ibid.
[638] Ibid.
[639] Ibid.
[640] Bueno above n 587 at 13.
[641] Ibid at 14.

depending on the outcome of these dicussions, the Swiss citizens may be called upon to vote on the initial Swiss Responsible Business Initiative later in 2020.

4.2.2 Norway

One example of legislation in Norway which is relevant for our purposes is the Norwegian law on gender parity in boards of public limited liability companies.

On 1 January 2006, section 6-11a of the *Norwegian Public Limited Liability Companies Act* was introduced, which made it compulsory for public limited liability companies to have at least a 40 per cent of women in their boards:

§ 6-11a. Requirement regarding the representation of both sexes on the board of directors

(1) On the board of directors of public limited liability companies, both sexes shall be represented in the following manner:

1. If the board of directors has two or three members, both sexes shall be represented.
2. If the board of directors has four or five members, each sex shall be represented by at least two members.
3. If the board of directors has six to eight members, each sex shall be represented by at least three members.
4. If the board of directors has nine members, each sex shall be represented by at least four members, and if the board of directors has more members, each sex shall represent at least 40 percent of the members of the board.
5. The rules in no. 1 to 4 apply correspondingly for elections of deputy members of the board of directors.

(2) The first paragraph does not apply to members of the board of directors who have been elected among the employees pursuant to § 6-4 or § 6-37 first paragraph. When two or more members of the board of directors as mentioned in the first paragraph are elected, both sexes shall be represented. The same applies to deputy directors. The provisions in the second and third sentence do not apply if one of the sexes is represented by less than 20 percent of the total number of employees in the company at the time of election.[642]

The entry into force was triggered by the inaction of the companies to introduce changes voluntarily, as it provided that the new wording would entry into force "only if companies did not, by 1 July 2005, in aggregate have 40 per cent representation by women on their boards".[643] The Act gave companies a two-year period to comply. Despite some protests, all the relevant companies complied with the period set. The standard applies to all public limited liability companies in Norway, but did not affect the composition of the boards of private companies.

In case of breach with the provision, the sanctions could vary from denial of registration in the Register of Business Enterprises to the dissolution of the company.

This example from Norway shows how human rights-related requirements could potentially be introduced into company law.[644] It also demonstrates how mandatory

[642] Allmennaksjeloven, lov av 13. Juni 1997 nr. 45 (Norwegian Public Limited Liability Companies Act of 13 June 1997 No 45), available in an unofficial English translation at the website of the Oslo Stock Exchange (Oslo Børs) at https://www.oslobors.no/ob_eng/Oslo-Boers/Regulations/Acts-and-regulations.

[643] Beate Sjåfjell, "Gender Diversity in the Board Room & Its Impacts: Is the Example of Norway a Way Forward?" *Social Science Research Network*, SSRN Scholarly Paper ID 2536777 28 (2014), available at: https://papers.ssrn.com/abstract=2536777.

[644] Ibid at 50.

legislation can bring about changes which voluntary mechanisms were unable to incentivise.[645]

Another development that is not yet legislative in nature is also of relevance. A Norwegian Ethics Information Committee was appointed to explore possible disclosure requirements relating to production sites used in manufacturing, as well as responsible business conduct and supply chain management.[646] If taken forward, this may entail an amendment to existing legislation, such as the Norwegian Environmental Information Act, or the proposal of a new law.

In November 2019, Norway released a draft Act relating to transparency in supply chains.[647] The draft legislation provides for a twofold duty: a "duty to know of salient risks that may have an adverse impact on fundamental human rights and decent work", which would apply to all companies offering goods or services in Norway, and a duty to disclose information about the company's adverse impacts on human rights and working conditions and significant risks thereof, and about its due diligence processes, as well as to actually undertake due diligence, which would be limited to larger companies.[648]

4.2.3 Canada

The Canadian Ombudsperson for Responsible Enterprises ("CORE") aims to review allegations of human rights abuses arising out from the operations of Canadian companies abroad. On the 8th of April, 2019, Sheri Meyerhoffer was appointed by the Minister of International Trade Diversification as the new Ombudsperson.[649]

Criticisms have been raised as to the lack of powers and independence granted to the Ombudsperson.[650] In particular, concerns were raised in relation to her lack of investigatory powers to compel documents or witnesses;[651] her lack of ability to recommend sanctions for companies that have been found to have caused, or contributed to, human rights abuses (such as the denial or withdrawal of trade advocacy support and future Export Development Canada financial support);[652] and the requirement for the reports prepared by the Ombudsperson to be provided to the Minister of International Trade (and to the Minister of Natural Resources for the reports concerning companies in the mining, oil or gas sectors) before being published.[653]

4.2.4 Australia

The Australian Modern Slavery Act entered into force on 1 January 2019. It requires companies carrying out at least part of their business in Australia (regardless of where

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645 Ibid.
646 Information on the Norwegian Ethics Information Committee is available at: https://nettsteder.regjeringen.no/etikkinformasjonsutvalget/norwegian-ethics-information-committee/.
647 Report from the Ethics Information Committee, appointed by the Norwegian government on June 1, 2018. Report delivered on November 28, 2019. Draft translation from Norwegian of sections of Part I. Available at: https://www.business-humanrights.org/sites/default/files/documents/Norway%20Draft%20Transparency%20Act%20-%20draft%20translation_0.pdf. See also BHRRC, "Norway: Government-appointed committee proposes human rights transparency and due diligence regulation", available at: https://www.business-humanrights.org/sites/default/files/documents/Norway%20Draft%20Transparency%20Act%20-%20draft%20translation_0.pdf
648 Ibid., Sections 5 and 10.
649 Global Affairs Canada "Minister Carr announces appointment of first Canadian Ombudsperson for Responsible Enterprise" (8 April 2019), available at : https://www.canada.ca/en/global-affairs/news/2019/04/minister-carr-announces-appointment-of-first-canadian-ombudsperson-for-responsible-enterprise.html.
650 Catherine Coumans, "Canada Still Needs an Ombudsperson to Investigate Mining Cases - Not an Advisor to the Minister of International Trade or another CSR Counsellor", *Miningwatch*, 4 May 2019, available at : https://miningwatch.ca/blog/2019/5/4/canada-still-needs-ombudsperson-investigate-mining-cases-not-advisor-minister.
651 Peter Mazereeuw, "Canada must 'walk the talk', give corporate ethics watchdog power to compel evidence: UN expert", *The Hill Times* (29 April 2019), available at: https://www.hilltimes.com/2019/04/29/canada-must-walk-the-talk-give-corporate-ombudsperson-more-powers-and-budget-un-expert/198285.
652 Coumans above n 650.
653 Ibid.

they are domiciled),[654] with a consolidated revenue of at least Aus$100 million to report disclose on the steps they have taken to identify and address risks of modern slavery, as well as how they assess the effectiveness of their actions.[655] The law establishes reporting criteria against which companies must report,[656] and statements must be approved by the "principal governing body" of the entity.[657] The Australian act also provides for the establishment of a government-run registry of statements: the Modern Slavery Statements Register,[658] but does not require the publication by the competent authorities of a list of entities required to report.

Chiara Macchi and Claire Bright have noted in relation to the Australian Modern Slavery Act that:[659]

> While the Australian Act can be seen as 'a step in the right direction', and relatively more advanced than the UK MSA, its effectiveness in contributing to the implementation of the UNGPs suffers largely from the same limitations highlighted for the UK MSA. In particular, it suffers from a lack of independent oversight and of effective machinery for enforcement with no penalties or civil liability regime envisaged in case non-compliance.

4.2.5 United States of America

The California Transparency in Supply Chains Act (the "California Act"),[660] adopted in 2010, requires certain companies to report on their efforts to combat slavery and human trafficking in their supply chains.[661] Studies which raise concerns around its effectiveness have been mentioned above.[662]

In addition, the US Trade Facilitation Act allows US Customs to seize imported goods if an importer is unable to provide a certificate proving which measures were taken ensure that the goods were not produced using forced labour.

In April 2019, a coalition of human rights and environmental civil society organisations proposed that the US Congress consider a draft Corporate Transparency Act, which would require disclosure of beneficial ownership for the purposes of addressing corruption, money-laundering and human rights and environmental harms.[663]

4.2.6 Brazil

In Brazil, two relevant developments are interesting for the purposes of due diligence. The first relates to a case which was successfully brought against Zara for human rights conditions in its supply chain. The second relates to the publication of the "Dirty List" of companies which have been alleged to have slavery conditions in their operations.

In 2011, the officers from the labour inspection of Brazil found 15 foreign workers working in two Sao Paolo workshops in conditions which the inspectors concluded to be

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[654] Sections 4-5 of the Australia Modern Slavery Act above n 512.
[655] Section 15(16)(1).
[656] Section 15(16).
[657] Section 15(13)(2).
[658] Section 17(18).
[659] Macchi and Bright above n 510.
[660] California Transparency in Supply Chains Act of 2010.
[661] The stated purpose of the Act is "to educate consumers on how to purchase goods produced by companies that responsibly manage their supply chains, and, thereby, to improve the lives of victims of slavery and human trafficking."
[662] Development International above n 505.
[663] Human Rights Watch, "US: Pass Law to Stem Corruption, Promote Rights: Act Would Require Companies to Disclose Real Owners" (11 April 2019), available at: https://www.hrw.org/news/2019/04/11/us-pass-law-stem-corruption-promote-rights.

analogous to slavery.[664] The workshops had been subcontracted by AHA, a major supplier of Zara Brazil at that time.[665] The authorities argued that Zara was the real employer and should be held legally responsible, as it exercised directive power over its supply chain.[666]

Following negotiations with labour prosecutors later that year, Zara Brazil and the authorities reached a Conduct Adjustment Agreement whereby Zara committed to a set of rules of conduct to avoid criminal proceedings to begin.[667]

A report by NGOs, SOMO and Repórter Brasil, noted that this was a novel approach by the Brazilian authorities, as Zara Brazil was one of the first textile companies to be held accountable for working conditions in an outsourced workshop.[668] The Agreement imposed on Zara an unprecedented obligation to audit its suppliers and subcontractors.

In Brazilian legislation, slave labour conditions occur:[669]

> [W]hen a worker is subjected to one or more of the following situations: forced labour; exhaustive working hours; degrading working conditions; restriction, by any means, of movement on account of debt contracted with the employer or agent, either when they are hired or over the course of the work contract; retention in the workplace by preventing the use of any means of transport, by maintaining overt surveillance and/or by confiscating personal documents or personal property.

As a result of the unfavourable publicity that employers receive from their inclusion in this public List, there have been fourteen challenges to the legality of the mechanism:

- In November 2004 the Confederation of Agriculture of Brazil challenged the constitutionality of the List in the Supreme Court.[670]

- In 2011, the Ministry of Labour and the Human Rights Secretariat renewed the List through an inter-ministerial order.[671]

- In 2014, following a challenge by the Brazilian Association of Real Estate Developers,[672] the Supreme Court suspended the publication of the List.

- In 2015, the Government issued a ministerial order[673] which clarified that employers could only be listed after the applicable administrative appeals had been exhausted. The publication of the List remained suspended.

- In 2016, an inter-ministerial order[674] provided employers with the possibility of signing a "Conduct Adjustment Agreement", which constituted a legal settlement. In this agreement, employers would commit to adjusting their conduct within a two-year-period. If they failed to do so, they could be included in the List.

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[664] André Campos, Mariëtte van Huijstee and Martje Theuws, "From Moral Responsibility to Legal Liability? Modern Day Slavery Conditions in the Global Garment Supply Chain and the Need to Strengthen Regulatory Frameworks: The Case of Inditex-Zara in Brazil", *SOMO and Repórter Brasil* (2015) 36, available at: https://www.somo.nl/wp-content/uploads/2015/05/From-moral-responsibility-to-legal-liability.pdf.
[665] Ibid at 34 and 36.
[666] Cees Van Dam, *Enhancing Human Rights Protection: A Company Lawyer's Business*, Rotterdam School of Management, Erasmus University (2015) at 36.
[667] Campos, van Huijstee and Theuws above n 664 at 38.
[668] Ibid at 39.
[669] Conectas "The back and forth of the slave labor dirty list in Brazil" (20 February 2018), available at: https://www.conectas.org/en/news/back-forth-slave-labor-dirty-list-brazil.
[670] Direct Claim on Grounds of Unconstitutionality (*Ação Direta De Inconstitucionalidade*) No. 3347.
[671] Inter-ministerial Order 2/2011.
[672] Direct Claim on Grounds of Unconstitutionality (*Ação Direta De Inconstitucionalidade*) No. 5209.
[673] Ministerial Order 2/2015.
[674] Inter-ministerial Order 4/2016.

- Also in 2016, the Supreme Court per Justice Cármen Lúcia Rocha closed the pending challenges against the List, declaring that the new rules for its publication were constitutional.

- Following this ruling, the Government of President Michel Termer announced it would not publish the List. The Office of the Public Prosecutor for Labour Issues challenged the President's decision and sought publication of the List. The Government appealed to the Superior Labour Court, and the President of the Court, Ives Gandra Martins Filho, granted an injunction to suspend the publication of the List again.

- In 2017, as a result of another appeal by the Office of the Public Prosecutor for Labour Issues the Superior Labour Court reviewed its previous ruling and ordered the publication of the List for the first time since 2014.

- Later in 2017, the federal government issued a ministerial order[675] which subjects the publication of the List to authorisation by the Ministry of Labour.

- In January 2018, the Brazilian Association of Real Estate Developers (Abrainc) filed another case with the Supreme Court to impede the publication of the List.[676] Abrainc argues that the publication of the List may only be regulated by a specific law, and not by a ministerial order. The case is pending.

Currently,[677] the publication of the Dirty List occurs every six months. It fell under the responsibility of the Ministry of Labour, but with the extinction of the Ministry of Labour, the List is meant to be published by the Ministry of the Economy.

4.3 Overview and Comparative Analysis of Country Reports

Robert McCorquodale*

4.3.1 Introduction

This project conducted a deep review of the relevant national laws and other regulation in relation to due diligence for human rights and environmental matters across 12 EU jurisdictions. These jurisdictions were: Belgium, Denmark; Finland; France; Germany; Ireland; Italy; the Netherlands; Poland; Spain; Sweden; and the United Kingdom. These detailed individual reports of each jurisdiction, written by experts in their field in each Member State, are set out in this Report.

This comparative analysis considers these individual reports and summarises the key elements of them. It does so through a framework which draws out some of the main aspects and trends of the individual reports in relation to human rights and environmental due diligence on companies.[678] It will first set out the areas of law in Member States in which due diligence has been applied, and what is the legal duty. It then considers the scope of this application in terms of the types of companies and the

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[675] Ministerial Order No. 1,129/2017.

[676] Claim on Grounds of Constitutional Infringement (*Arguição de Descumprimento de Preceito Fundamental*) No. 509

[677] Following the suspension of Ministerial Order No. 1,129/2017 by Justice Rosa Weber at the Supreme Court.

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[678] The terminology of "companies" is used here as it is the term generally used in these Country Reports. The legislation is summarised and abbreviated in this chapter as the full terminology of the legislation can be found in the individual Country Reports. The footnotes cited in this section contain the original formatting provided by the experts in their Country Reports. For further details please see the individual Country Reports in Part III Country Reports.

areas of human rights and environment covered, and if it is applied transnationally. It will examine the application of this to corporate groups and others, followed by consideration of the monitoring, enforcement and remedies across the jurisdictions, with comments on the links to EU laws where relevant. This comparative analysis is primarily in relation to existing laws in these Member States, with some reflections on proposed laws.

4.3.2 Areas of law

The breadth of the areas of national law which have aspects of due diligence for human rights and environmental matters is extensive. It primarily includes many areas of corporate law, such as general company law and laws regarding financial statements,[679] as well as in stock exchange listing requirements[680] and in money-laundering legislation.[681]

Other areas of law for which most Country Reports noted that they had some form of human rights and environmental due diligence requirements, were health and safety law,[682] product liability law,[683] employment law[684] and environmental law.[685] Some Country Reports traced due diligence requirements to their constitutional and public law,[686] consumer law,[687] equality law,[688] and bribery law,[689] as well as in the consideration of public procurement law.[690] In addition, there is the Vigilance Law in France,[691] which is legislation specifically focussed on due diligence for human rights and environmental impacts, as well as the Child Labour Due Diligence Law in The Netherlands[692] and Modern Slavery Act in the United Kingdom, both of which cover a more limited range of human rights.[693] There is also a proposal in Germany for a broad-based mandatory due diligence law.[694]

These Country Reports indicate that some Member States have chosen a regulatory method that is less legislation based. This includes The Netherlands' approach to specific sector guidance[695] and the Danish approach to export credit.[696] Most Member States have corporate governance codes, which are not legally binding but highly influential in the area of due diligence.[697] There is also regulation on the broad area of corporate social responsibility (CSR) in some Member States – which is often confused with specific

[679] For example, Denmark's Financial Statements Law, Ireland's Companies Act, Spain's Law amending the Commercial Code and Sweden Annual Account Act.
[680] For example, Spain's Royal Legislative Approving the Consolidated Text of the Law of the Stock Market.
[681] For example, Sweden's Money Laundering and Terrorist Financing (Prevention) Act and United Kingdom's Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations.
[682] For example, Finland's Consumer Safety Act, Italy's Consolidated Text on Health and Safety at Work and United Kingdom's Food Safety Act.
[683] For example, Germany's Act on Liability for Defective Products.
[684] For example, Poland's Act amending the Labour Code, Spain's Law on Prevention of Occupational Risks and the United Kingdom's Equality Act.
[685] For example, Germany's Water Resources Act, Italy's Law on Decontamination of Polluted Sites and Poland's Environmental Damage Act.
[686] For example, Article 45 of the Spanish Constitution and Denmark's Act on a Mediation and Complaints-Handling Institution for Responsible Business Conduct.
[687] For example, United Kingdom's Consumer Protection Act.
[688] For example, Ireland's Human Rights and Equality Commission Act.
[689] For example, United Kingdom's Bribery Act.
[690] For example, Denmark's Public Procurement Act, Germany's Law against Restraints of Competition and Finland's Act on Public Procurement and Concession Contracts.
[691] France's Law No 2017-399 of 27 March 2017 (Vigilance Law).
[692] The Netherlands Child Labour Due Diligence Act 2019.
[693] United Kingdom's Modern Slavery Act 2015.
[694] Draft German Law on Corporate Human Rights and Environmental Due Diligence in Global Value Chains 2019.
[695] For example, The Netherlands' international responsible business conduct (IRBC) Agreement on Sustainable Garment and Textile. See also the German Partnership for Sustainable Textiles.
[696] See Danish Institute of Human Rights, Erhverv og menneskerettigheder i en dansk kontekst (2016) 25.
[697] For example, Belgium's Code on Corporate Governance and Spain's Good Governance Code of Listed Companies.

human rights regulation[698] – with a range of non-binding initiatives.[699] These Country Reports all consider relevant developments in relation to tort and contract law that can be either legislative based or in case law,[700] and within criminal law.[701]

Throughout the Country Reports it is evident that Member States have brought in legislation specifically to implement EU law. The main area where this is evident is the inclusion in each Member State of corporate law in relation to non-financial reporting. In each case, this has been due to the influence of the EU Directive on Non-Financial Reporting.[702] Yet it is also clear that many other relevant national laws have been passed due to EU laws.[703]

It is, therefore, evident that human rights and environmental due diligence is a practice and process that is applied in many and diverse laws across Member States, and is not at all unfamiliar in these national laws. This due diligence is expressly related to human rights and environmental matters, even if not always using the specific term of "human rights due diligence".

4.3.3 The Legal Duty

The focus of the Country Reports is on those national laws and other regulations which are relevant to human rights and environmental due diligence. It is evident from these 12 Country Reports that the terminology of the regulations varies considerably in this regard. The legal duty on companies has been expressed, for example, as a duty to respect, a duty to prevent, a duty to meet a certain standard, a duty to implement process, a duty to report and a duty of care.

A useful example of this diversity of uses of due diligence obligations on companies is that of German law. As set out in the German Country Report, the German legal order contains examples of different types of due diligence obligations, including precautionary duties, supervision duties, protective duties and safety duties, whose concrete scope and content is tailored to the respective purpose of the law and the risks it aims to address. All these due diligence obligations are subject to standards of reasonableness, appropriateness, adequacy, cost-benefit analysis, etc., which ultimately give effect to the proportionality principle that the measure deployed is not out of proportion with the goal pursued. This entails that the more severe a measure interferes with human rights and the environment, the weightier is the public interest in regulation. These due diligence standards are fleshed out in German law with regard to the type of risk to be addressed, the likelihood and severity of the impact or damage to be expected, and the economic costs involved in minimising or excluding the risk. In this regard, the specific precautionary duties in environmental law aim to address risks whose materialisation is possible yet not sufficiently probable to trigger a more robust duty of protection.[704] This is of particular importance where the damage may prove irreversible.

In addition, under German law corporate due diligence obligations are limited by a notion of "adequacy" [*Angemessenheit*] that applies at the risk analysis stage. In German law, adequacy requires a proportionate relationship between means and ends.

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[698] On the difference between CSR and human rights, see, for example, Karin Buhmann, Jonas Jonsson and Mette Fisker, "Do No Harm and Do More Good Too: Connecting the SDGs with Business and Human Rights and Political CSR Theory, *Corporate Governance*, November 2018.
[699] For example, Denmark's CSR Compass and Spain's CSR Strategy.
[700] For example, Germany's Due Diligence Obligations in the Law of Non-Contractual Obligations, Belgium's general contract law, and United Kingdom's common law.
[701] For example, Italy's Administrative Responsibility of Legal Entities, Companies and Associations Act.
[702] EU Directive on Non-Financial Reporting, EU Directive 2014/95/EU.
[703] For example, Directive 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and Directive 89/391 on labour rights.
[704] Such as laid down in Article 5 I(1) No 2 of the Act on the Protection of Humans, Animals and the Environment against Harmful Emissions.

In relation to due diligence, there are some examples in the Law regulating the Credit System, which provides that "*proper business administration must include adequate and effective risk management, on the basis of which the credit institute must continuously ensure its risk-bearing capacity"*,[705] and the Money Laundering Act, where companies have to demonstrate that the scope of due diligence measures taken is "adequate" in relation to the risks of money laundering and terrorist financing.[706] In the proposed German Legislation on Corporate Human Rights and Environmental Due Diligence in Global Value Chains, it specifies that in order to satisfy the requirement of adequacy, business enterprises have to conduct an "enhanced risk analysis" whenever they become aware of concrete risks of human rights impacts.[707]

Polish law has another concept being that of due care [*należyta staranność*].[708] As explained in its Country Report, it is due care that the Polish legal system most often identifies as an objective criterion for assessing the behaviour of an entity to which to attribute liability for non-performance or improper performance of an obligation, or for tort or delict. The standard must take into account the special ability to predict pre-emptiveness and reliability in the way a professional works, and the large requirements in terms of their knowledge and practical skills or professionalism. It should be emphasized that it is also about the knowledge that goes beyond the scope of specialist information in a given field but is essential for professional activity.[709]

In contrast, the terminology in The Netherlands Child Labour Due Diligence Act is expressly that of "due diligence". As set out in the Netherlands Country Report, there is a requirement for the companies involved to conduct due diligence [*gepaste zorgvuldigheid*] with a view to preventing child labour from being used in the production of the goods and services they supply to Dutch end-users, as part of consumer protection (rather than about transparency). According to the Act:

[t]he company that … investigates whether there is a reasonable presumption that the goods and services to be supplied have been produced using child labour, and that draws up and carries out an action plan in case there is such a reasonable presumption, conducts due diligence.[710]

The due diligence requirement is not defined further in the Act, other than it mentions that more detailed requirements with respect to both the investigation and the action plan will be set by General Administrative Order, taking account of the existing International Labour Organization's Child Labour Guidance Tool for Business.[711] Interestingly, the term "due diligence" (in Dutch and English) is used for the Dutch international responsible business conduct (IRBC) Covenants.

In contrast, the French Vigilance Law does not use the term "due diligence". The France Country Report notes that the vigilance obligations under the Vigilance Law shares commonalities with the human rights due diligence process provided by the United Nations Guiding Principles on Business and Human Rights (UNGPs) and the OECD Guidelines for Multinational Enterprises. Indeed, it is accepted that these were inspirations for the Vigilance Law.[712] Yet, these vigilance obligations and the UNGP's due

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[705] Article 25a I, Geran Law regulating the Credit System. What is required for adequate risk management depends on the type, scope, complexity, and risks inherent in the business activity.
[706] Article 15, German Money Laundering Act.
[707] Article 5 III, proposed German Legislation on Corporate Human Rights and Environmental Due Diligence in Global Value Chains.
[708] Article 355(1) of the Polish Civil Code.
[709] See A. Olejniczak. *Art. 355*, in A Kidyba (ed) *Kodeks cywilny. Komentarz. Tom III. Zobowiązania - część ogólna* (2nd edition, LEX, 2014).
[710] Article 5(1), The Netherlands Child Labour Due Diligence Act.
[711] Ibid, Article 5(2).
[712] See Stéphane Brabant, Elsa Savourey and Charlotte Michon, The Vigilance Plan: Cornerstone of the Corporate Duty of Vigilance Law, International Review of Compliance and Business Ethics *Revue Internationale de la Compliance et de l'Ethique des Affaires* December 2017, p.4.

diligence are not considered to be identical. Companies within the scope of the Vigilance Law have to establish a vigilance plan setting out: [713]

> [R]easonable vigilance measures adequate to identify risks and to prevent severe impacts on human rights and fundamental freedoms, on the health and safety of persons and on the environment, resulting from the activities of the company and of those companies it controls within the meaning of II of article L. 233-16, directly or indirectly, as well as the activities of subcontractors or suppliers with whom there is an established commercial relationship, when these activities are related to this relationship.

This terminology refers to "reasonable vigilance measures" [*mesures de vigilance raisonnable*], rather than the UNGPs procedural terminology [*procédure de diligence raisonnable*]. In addition, the term "vigilance" is preferred in French law to "duty of care", on the basis that the common law duty of care does not exist in France.

The duty of care does exist in the United Kingdom in tort law, as a company may be found liable in negligence if it is established that the company owed a duty to the claimant, it then breached that duty and caused the claimant to suffer loss which is recoverable. The United Kingdom's Supreme Court has found that a parent company can owe a duty of care to those harmed by the actions of its foreign subsidiary, on the basis that:[714]

> [T]here is nothing special or conclusive about the bare parent/subsidiary relationship, it is apparent that the general principles which determine whether A owes a duty of care to C in respect of the harmful activities of B are not novel at all.

Nevertheless, as stated in the United Kingdom's Country Report, some United Kingdom regulation does refer directly to due diligence, for example, an obligation to take reasonably practicable steps to avoid a harm to a stakeholder, or as part of a failure to prevent obligation (such as under the United Kingdom Bribery Act) or as a defence to the occurrence of a liability. A key feature of "due diligence" in all of these different contexts in the United Kingdom is the element of objectivity. In other words, in each case risk management steps taken by a company to avoid liability accruing under a law will not amount to "due" diligence unless it meets an objective standard (yet to be clearly defined). It is apparent that any due diligence carried out by a company must be proportionate to the risks of the unwanted event occurring, taking into account the business' complexity, size and operating context.[715]

Other Member States have laws which use due diligence in a variety of ways. For example, in the Spain Country Report, it is noted that in the Spanish law on the Prevention of Money Laundering and Terrorist Financing the term "due diligence" [*diligencia debida*] is used and that there is, depending on the risk, different levels of application of due diligence measures: normal due diligence; simplified due diligence; and enhanced due diligence measures. In normal due diligence, a company shall conduct ongoing monitoring of the business relationship, including scrutiny of transactions undertaken throughout the course of that relationship to ensure that the transactions being conducted are consistent with their knowledge of the customer, the business and risk profile, including the source of funds and to ensure that the documents, data and information held are kept up-to-date.[716] Simplified due diligence measures apply with

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[713] Vigilance Law; Commercial Code, article L. 225-102-4.-I.
[714] *Vedanta Resources plc v Lungowe and Others* [2019] UK SC 20, paragraph 54.
[715] See UN Guiding Principle 17(b), which provides that human rights due diligence will "*vary in complexity with the size of the business enterprise, the risk of severe human rights impacts, and the nature and context of its operations*".
[716] Article 6, Prevention of Money Laundering and Terrorist Financing.

respect to those customers, products or transactions that involve a low risk of money laundering or terrorist financing, and enhanced due diligence applies where the risks are high. In contrast, under the Italian law on Health and Safety at Work, the focus is on risk assessment, where, in order to assess the risks of a work situation, it is necessary to carry out a form of due diligence that identifies all the dangers connected with the activity carried out and quantifies the risk, that is the probability that each danger turns into an adverse event, taking into account the entity of the potential damage. [717]

Similar to the position in the United Kingdom, a defence of due diligence is available under certain Italian laws, such as in the case of a crime committed by a company's representatives or employees.[718] This defence of due diligence is recognised in Finnish law[719] and the Irish Criminal Justice (Corrupt Offences) Act, provides that "*it shall be a defence for a body corporate against which such proceedings are brought to prove that it took all reasonable steps and exercised all due diligence to avoid the commission of the offence*".[720]

Overall, there are a variety of terms used in national law for due diligence in relation to human rights and environmental matters. Even where the terminology of "due diligence" is not used, the intent is to place a legal obligation on a company to undertake a risk assessment, with clear processes, and with the risk to those other than the company – being employees, consumers, and other stakeholders – as the main focus. It is, therefore, evident that a use of the term "due diligence" in relation to human rights and the environment in any EU legislation would not be a problem for harmonisation within the Member States surveyed.

4.3.4 Scope

The issue of scope of these national laws on due diligence concerns the type and size of companies covered by the laws and the breadth of human rights and environmental matters included. One of the most extensive of these laws is found in Italy's Administrative Responsibility of Legal Entities, Companies and Associations Act, which applies to all "*corporate entities and companies and associations, regardless of whether they have legal personality*",[721] other than state bodies, and to those human rights and environmental violations which are also crimes.[722] Similarly, Italy's health and safety law provides that the Risk Assessment Document is mandatory for all companies that have at least one employee or one collaborator, and must be drawn up within 90 days for a new activity.[723]

Other national laws limit their scope to certain sizes of companies. For example, the French Vigilance Law provides that the following companies are included within its scope:[724]

> Any company that employs, by the end of two consecutive financial years, at least five thousand employees itself and in its direct or indirect subsidiaries whose registered office is located within the French territory, or at least ten thousand employees itself and in its direct or indirect subsidiaries whose registered office is located within the French territory or abroad, shall establish and effectively implement a vigilance plan.

[717] Articles 17, 28 and 29, Italy's Law on Health and Safety at Work.
[718] Italy's Administrative Responsibility of Legal Entities, Companies and Associations Act.
[719] Finnish Act on Compensation for Environmental Damage, Section 7.
[720] Section 18(2), Irish Criminal Justice (Corrupt Offences) Act. See also section 10 of the Irish Employment (Miscellaneous Provisions) Act.
[721] Article 1, Italy's Administrative Responsibility of Legal Entities, Companies and Associations Act.
[722] Ibid, Article 25.
[723] Article 4, Italy's Health and Safety Law.
[724] Commercial Code, article L. 225-102-4.-I, as introduced by France's Vigilance Law.

In addition, the company's vigilance plan must include "*severe impacts on human rights and fundamental freedoms, on the health and safety of persons and on the environment*".[725] In contrast, The Netherlands Child Labour Due Diligence Act applies to every company, whether domiciled in the Netherlands or not, and whether listed or not, which supplies goods or services to Dutch end-users, being *"the natural or legal persons that use or use up the goods or make use of the services"*.[726] Also included are foreign companies that have a branch or structurally conduct business in the Netherlands,[727] though it excludes companies that only transport the goods.

However, the proposed German Legislation on Corporate Human Rights and Environmental Due Diligence in Global Value Chains seems to apply just to "major companies", though it can extend to "other companies" and subsidiaries controlled by their parent company, provided these companies (a) operate in a "high risk sector", being defined as agriculture, forestry and fishery; mining; manufacturing industries, including food, textile and electronics; and energy supply or (b) operate in conflict-affected or high-risk areas.[728] Its human rights scope is expansive as it includes all "internationally recognised human rights" (listed in an annex) and "basic environmental requirements", which cover any environmental legislation of the State where the damage occurs and international treaties that bind Germany. By comparison, the scope of companies within the United Kingdom's Modern Slavery Act is limited by turnover, as it only applies to a company which carries on a business, or part of a business, in the United Kingdom, supplies goods or services and has an annual turnover of £36 million or more (globally).[729] The Act also deals solely with slavery, servitude and forced or compulsory labour, as well as human trafficking.

In relation to corporate law more generally, every Member State has implemented the EU Directive on Non-Financial Reporting, with almost all adopting the full scope of the Directive.[730] Accordingly, in most Member States listed companies with 500 employees or more are required to provide a report, though Denmark and Sweden extend this by requiring companies with 250 employees or more, including state companies, or having a certain turnover, to prepare a report. Some Member States have extended the Directive's scope in other ways, as France includes some unlisted companies that are above certain financial and employee thresholds, Spain includes public interest financial companies (such as banks, insurance companies, investment fund managers and pension funds), and Italy includes some turnover aspects to extend its scope (20 million euros of total assets from the balance sheet, and/or 40 million euros from revenues net sales). All of the Member States in this Report require companies to report on the same environmental, social or governance factors, though France and Italy's scope in this regard are slightly broader.[731]

Some Member States specifically extend the obligations of due diligence to state or public sector companies. For example, the Irish Human Rights and Equality Commission Act requires public entities to undertake human rights due diligence, and those duties extend to all government departments, local authorities, and other public authorities, and also to companies "wholly or partly financed" or where a majority stake is owned by the Irish government.[732] Similarly, Sweden requires state-owned companies' boards of

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[725] Legislative Decree 9 April 2008, n. 81 Consolidated Text on Health and Safety at Work, para. 3.
[726] Child Labour Due Diligence Act, Preamble.
[727] Article 5d, Dutch Commercial Register Act.
[728] Article 3, proposed German Law on Corporate Human Rights and Environmental Due Diligence in Global Value Chains.
[729] Section 54(2), United Kingdom's Modern Slavery Act.
[730] See GRI and CSR Europe, Policy & Reporting: Member State Implementation of Directive 2014/95/EU (2018), https://www.globalreporting.org/resourcelibrary/NFRpublication%20online_version.pdf.
[731] For a useful summary, see Frank Bold, *Comparing the Implementation of the Non-Financial Reporting Directive* (2017), http://www.purposeofcorporation.org/comparing-the-eu-non-financial-reporting-directive.pdf.
[732] Irish Human Rights and Equality Commission, *Public Sector Equality and Human Rights Duty- FAQ, available at:* https://www.ihrec.ie/our-work/public-sector-equality-and-human-rights-duty-faq/.

directors to define and adopt sustainability targets and integrate sustainable business into their business strategies.[733]

In other specific areas of regulation, the scope of the legislation tends to cover all companies, such as in the areas of health and safety, and the environment, or for a range of industry sectors. For example, in Spain an environmental impact assessment is required for the following sectors: intensive livestock installations; extractive industry; mineral and steel industries. production and processing of metals; chemical, petrochemical, textile, paper industries industry; infrastructure projects; hydraulic engineering and water management projects; waste disposal and recovery projects; and other projects developed in sites protected under the Natura 2000 Network and in protected areas by international instruments.[734] In relation to the different approach to regulation in this area in The Netherlands, there are eight IRBC covenants which are operational. They apply to certain sectors: garments and textile; banking; the gold sector; the insurance sector; pension funds; sustainable forestry; the food products sector; and a pilot on natural stone. The different covenants differ in scope, with some focusing on human rights impacts only (e.g. in banking) and others focusing on a broader range of issues, including impacts on the environment, health and safety, living wage and animal welfare (e.g. in garments and textile).[735]

Therefore, there is diversity in the scope of these regulations on human rights and environmental due diligence across the Member States surveyed. While the UNGPs include all business enterprises and core international human rights law as being part of the responsibility to undertake human rights due diligence,[736] this survey shows that across all these Member States there is a minimum scope which includes all listed private companies of a certain size (in terms of employees or turnover), and the relevant national and international human rights and environmental law are included within their scope. There are, though, many examples of considerably broader scope found in national law.

4.3.5 Transnational Application

Most laws within Member States are limited in scope and application to the territory of the Member State. However, the Country Reports indicate that there are a range of laws which concern due diligence which do operate transnationally (i.e. extraterritorially).

In most instances where there is transnational application, the national law requires companies which are domiciled within their territory to report on activities which they have undertaken outside the territory. This includes France's Vigilance Law, The Netherlands Child Labour Due Diligence Act and the United Kingdom's Modern Slavery and Bribery Acts, as well as the proposed German Legislation on Corporate Human Rights and Environmental Due Diligence in Global Value Chains. In each instance, the relevant law effectively includes the actions of subsidiaries, subcontractors and suppliers which may be based outside the territory of the Member State but which are in a business relationship with the relevant company domiciled in that Member State. This reference to "domicile" in national regulation is drawn directly from the EU Brussels I Recast Regulation, which is not limited to companies incorporated in the Member State, as it includes those companies with their central administration and principal place of business within that Member State.[737]

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[733] Government offices of Sweden, The State's Ownership Policy and Guidelines for State-Owned Enterprises (2017) 5.
[734] Spanish Law on Environmental Assessment.
[735] See The Netherlands Country Report.
[736] For example, Guiding Principles 11 and 12.
[737] Regulation (EU) No 1215/2012 of the European Parliament and of the Council of 12 December 2012 on Jurisdiction and the Recognition and Enforcement of Judgments in Civil and Commercial Matters.

The Netherlands Child Labour Due Diligence Act would seem to extend this breath of application further to include companies registered outside the jurisdiction and which supply goods or services to Dutch end-users, even if The Netherlands is not their principal place of business or central administration. There is a different development in Spain. Its Law on External Action and Service of the State, requires that State companies when operating outside Spain, should act in accordance with human rights, and that these companies must be socially responsible, particularly in transnational business.[738]

Some other national laws extend transnationally, for example, to employees of domiciled companies who are working outside the territory.[739] In addition, the Italian Law on Administrative Responsibility of Legal Entities, Companies and Associations[740] extends its criminal corporate liability jurisdiction to crimes committed outside Italy by Italian companies, including for specific transnational organised crimes. This extension includes foreign subsidiaries of Italian companies if the violation occurred partly in Italy and partly abroad.[741] The German Act against Restraints of Competition enables the competent authorities to take into account and regulate conditions for the provision of the law outside the German domestic jurisdiction.[742]

There is considerable national law within the Member States surveyed which applies the due diligence obligations in human rights and environmental matters to all companies incorporated or registered in that Member State, as well as companies whose principal place of business or central administration is within that Member State. This application is what has been called "domestic measures with extraterritorial implications",[743] as it regulates a wide range of companies operating within a Member State while having a transnational effect. While some national law extends this transnational application, nevertheless the laws in these Member States clearly indicate that some transnational application of these due diligence obligations is now widely accepted in the EU.

4.3.6 Corporate Groups

A key issue in considering the use and application of human rights and environmental due diligence is the means by which national laws determine what is the "company" for which the due diligence obligation applies. This is within the context of the use of the term "business enterprise" by the UNGPs to include a broad range of corporate structures, and the term "business relationship" to cover the various types of contractual and other links that companies have worldwide.[744]

It is clear from all the Member States surveyed that national law often applies to a broad corporate group (as a business enterprise). This is evident in the implementation of the EU Non-Financial Reporting Directive, where all Member States have applied it to the corporate group, which extends beyond the company itself. For example, in the United Kingdom, parent companies must prepare a consolidated strategic report for all of the companies in the group.[745]

Similarly, in relation to the OECD National Contact Points, the company for which a complaint can be made generally includes its subsidiaries. In some instances, such as in Denmark, "business associates" are expressly included, meaning business partners,

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[738] Spanish Law on External Action and Service of the State.
[739] See, for example, Spanish Law on Prevention of Occupational Risks, contra Danish Working Environment Act.
[740] Italy's Administrative Responsibility of Legal Entities, Companies and Associations Act.
[741] Ibid at article 4.
[742] Article 128, German Act against Restraints of Competition.
[743] Office of the High Commissioner for Human Rights, *Business and Human Rights: Further Steps towards the Operationalisation of the 'Protect, Respect, and Remedy Framework'*, A/HRC/14/27 (2010) para 55.
[744] See UNGPs, Guiding Principle 13.
[745] Section 414A(3), United Kingdom Companies Act.

entities in the supply chain, and other non-public or public entities that can be related directly to the business activities, products or services of the company, authority organisation.[746] The United Kingdom's Bribery Law also extends its application to companies for the actions of "business associates", being any person who performs services for or on behalf of the organisation (and may include an employee, agent or subsidiary),[747] which could even include a supplier.[748] Further, the specific sector covenants in The Netherlands refer to the UNGPs and OECD Guidelines, in stating that *"enterprises bear a responsibility for preventing and reducing any adverse impact on people and the environment by their own operation or business relationships in the production or supply chain"*.[749]

The French Vigilance Law includes within its coverage a company and the activities of "*companies it controls within the meaning of II of article L. 233-16, directly or indirectly, as well as the activities of subcontractors or suppliers with whom there is an established commercial relationship, when these activities are related to this relationship*",[750] as well as French registered subsidiaries of foreign companies. This legislation uses a threefold definition of the concept of "control", being legal, de facto, or contractual, as linked to consolidated and group management reports.[751] In addition, the Vigilance Law does not refer directly to subcontractors and suppliers within the supply chain but relies on established commercial relationships as being the key factor.[752]

A different approach is found in The Netherlands Child Labour Due Diligence Act, where the scope of the obligations imposed on these companies under the Act is not limited to certain tiers of the supply chain. Rather, as the companies involved are expected to investigate whether there is a reasonable presumption that the goods and services to be supplied have been produced using child labour, it means that they would have to review their entire supply chain. As the suppliers can provide a declaration with respect to those goods or services along the lines, this should have the effect of moving these obligations down the supply chain. Similarly, the United Kingdom's Modern Slavery Act expressly references modern slavery in supply chains as being relevant to a company's statement published under the provision,[753] and the guidance to the Act recognises that for these purposes subsidiaries can form part of a parent company's "own business or supply chain".[754]

This broader view of corporate group having a due diligence obligation can also be seen in general contract law. For example, the Country Report on Belgian law notes that a third party, such as employees of a debtor, can be given the right to enforce a contractual provision concerning their labour conditions, and a code of conduct concerning human rights or supply chain due diligence can be inserted across the whole chain by a "chain clause" [*kettingbeding*][755] which obliges the contracting party to insert a certain obligation in a subsequent contract, coupled with the obligation to let any subsequent contracting party insert it as well. The enforceability of this clause can be strengthened by adding a provision in favour of a third party, namely the first creditor, and a damages clause. The first creditor can then enforce the obligation against any sub-supplier who has accepted this provision.

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[746] Section 3, Danish Act on a Mediation and Complaints-Handling Institution for Responsible Business Conduct.
[747] Section 8, United Kingdom Bribery Act.
[748] United Kingdom Bribery Act Guidance, page 16: *"where a supplier can properly be said to be performing services for a commercial organisation rather than simply acting as the seller of goods, it may also be an 'associated' person".*
[749] See The Netherlands, IRBC Agreement on Sustainable Garment and Textile, p. 8. According to the Agreement, the chain consists of six stages: 1) production of raw materials and fibres; 2) manufacture of materials (textiles) from yarn, including weaving, knitting, braiding, tufting, finishing and dyeing stages; 3) manufacture of components such as buttons, zips and garment trimmings; 4) manufacture of garments; 5) product design and development (often for brands); and 6) retail trade.
[750] Commercial Code, article L. 225-102-4.-I as introduced by the Vigilance Law.
[751] Ibid at article L. 233-16.-II.
[752] See, Sherpa, Vigilance Plans Reference Guidance, Feb. 2019 at 32-33.
[753] Section 54(5), United Kingdom's Modern Slavery Act.
[754] United Kingdom's Modern Slavery Act Guidance at 23.
[755] See V. Sagaert, *Goederenrecht. Beginselen van Belgisch Privaatrecht,* Kluwer (2014).

In tort law, the position in the EU seems to be that there is corporate liability of parent companies for subsidiaries in tort law across Member States, as was stated by the Polish courts.[756] This is confirmed in Dutch courts[757] and by United Kingdom courts,[758] which would suggest a case might succeed against a defendant company where the company's supplier caused harm to the claimant, provided the claimant could establish that the company "*intervened in the management of the supplier's activities*"[759] in such a way as to assume a duty of care to the claimant. Of course, any claim under tort law across all EU Member States requires evidence and proof of causation to be successful.

A different approach is found using vicarious liability, especially in employment law, of the parent company for actions and omissions of its subsidiary. This is seen across a range of Member States, such as in Belgium[760] and Spain.[761] Other areas of law, such as on health and safety, have aimed to incentivise due diligence in human rights and the environment by companies over the operations of their subsidiaries and suppliers by extending criminal liability to entities which simply sell or supply defective or harmful products.[762]

It is evident from these Country Reports that there is now a general practice across Member States to include subsidiaries within the corporate group for which due diligence obligations in human rights and the environment apply. In many instances, the existence of the legal relationship between a parent company and a subsidiary is the key factor, though evidence of particular control may be required in some laws. In addition, there is a growing list of national laws and decisions which specifically include suppliers as part of the company's obligations to act with due diligence in human rights and environmental matters.

4.3.7 Monitoring, Enforcement and Remedies

Across all Member States surveyed, there were monitoring bodies, enforcement mechanisms and remedies available for many of the national laws related to due diligence in human rights and environmental matters. These do, though, vary considerably in their degree of monitoring, the effectiveness of the enforcement mechanisms and the remedies available.

In many instances, the monitoring of the obligations is done by private actions by individuals (as shareholders or other stakeholders) and civil society or by public actions by regulators, with the judicial system as the final process.[763] In some Member States it is a combination of public and private enforcement of corporate due diligence obligation which operates. For example, in Germany the Administrative Offences Act authorises public authorities to impose fines on business owners (and even their directors) for failure to comply with their monitoring and supervision obligations with regard to compliance with legal duties contained in other areas of law and addressed to them in

[756] Verdict of the Court of Justice (Ninth Chamber) of 20 June 2013 in Case C-186/12, and Polish Supreme Court judgment of 24 November 2009, V CSK 169/09. Note also the draft of a Polish Act on Specific Responsibility of Parent Companies for Damages to the Dominated Company, its Partners and Creditors, where "*a parent company will be obliged to repair the damage resulting from the abuse of a dominant position unless it proves the lack of guilt*": *Podmiot dominujący będzie musiał naprawić szkodę firmie zależnej lub jej pracownikowi*, Rzeczpospolita (25th April 2019), available at: https://www.rp.pl/Firma/304259988-Spolki-matki-zaplaca-za-corki---o-projekcie-ws-odpowiedzialnosci-za-szkody-w-spolce-kapitalowej.html.
[757] See *Akpan v Royal Dutch Shell PLC* Arrondissementsrechtbank Den Haag, 30 January 2013 Case No C/09/337050/HA ZA 09-1580.
[758] *Vedanta Resources plc v Lungowe and Others* [2019] UK SC 20.
[759] Ibid at para 44.
[760] Article 1384, third limb Belgium Civil Code.
[761] See Spanish Supreme Court, judgment of 28 May 1984, Civil Division (RJ 1984/2800).
[762] See Section 12(1), United Kingdom Consumer Protection Act. This is subject to the due diligence defences.
[763] See, for example, Spain's Law on Prevention of Occupational Risks and its Law on Environmental Assessment.

their capacity as business owners,[764] while the German Civil Code enables private litigants to claim damages for violations of due diligence obligations contained in other laws, provided these laws also aim to protect individual interests.[765] Sometimes, it is the company itself which is meant to monitor its own compliance, such as with the Danish Financial Statements Act, which operates with a "follow-or-explain" principle.

In some national laws the obligation on companies is one of strict liability, regardless of negligence or deliberation by a company, and there is automatic enforcement. One example is the Finnish Act on Compensation for Environmental Damage, where there is strict liability on companies for environmental damage towards anyone affected.[766] Sometimes there is a reverse burden of proof, such as under the German Civil Code in relation to health and safety, which creates a form of negligence liability with a reversed burden of proof, in that a company incurs liability for damages unlawfully caused by vicarious agents unless it can prove that it exercised due diligence in selecting, equipping or supervising these agents; or that the damage would have occurred in spite of exercising the required due diligence.[767]

Where there is a specific national law on human rights and environmental due diligence, they tend to add some different dimensions to these issues of monitoring, enforcement and remedies. The French Vigilance Law does not have a specific monitoring body but it does provide for civil liability under tort law where the company breaches its own vigilance obligations.[768] The three conditions for civil liability applicable under French tort law - and for which the claimant has the burden of proof - are the existence of damage, a breach of or the failure to comply with the vigilance obligation, and a causal link between the damage and the breach.[769] The more remote in the supply chain that the damage occurred, the harder it might be for the claimant to prove that the damage has occurred as a result of a breach of the vigilance obligations, that there is causal link between such a breach and the resulting damage, and that they are within the scope of the vigilance obligations. If the claimant is successful, then the court can order specific performance and compensation for actual harm. More generally, if a company has failed to comply with its vigilance obligations, it is given a three months' official notice to comply – for which a non-governmental organisation and trade union can apply as it does not need to be a claimant – and failure in complying with this notice leads to fines on the company.[770] There is no separate civil liability under the Vigilance Law for the parent company based on the fault of other entities in their supply chains and there is no criminal liability.[771]

In contrast, under The Netherlands Child Labour Due Diligence Act any natural or legal person (such as a consumer or competitor) whose interests have been affected by the (in)actions of a company in complying with the provisions as set out in the Act can file a complaint with the public supervisor (who has yet to be appointed).[772] If the company does not comply with the supervisor's order, the supervisor can impose administrative fines of up to €8,200 for non-compliance with the duty to file a declaration, and of up to €820,000, or up to 10% of the company's annual turnover, for non-compliance with the duty to conduct due diligence.[773] The proposed German Legislation on Corporate Human Rights and Environmental Due Diligence in Global Value Chains has a similar range of fines against companies (with a minimum of €250,000), with the additional penalty of

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[764] Article 130 Administrative Offences Act. See also the Posted Workers Act and the Water Resources Act.
[765] Article 823 II German Civil Code.
[766] Section 7, Finnish Act on Compensation for Environmental Damage.
[767] Article 831 German Civil Code. See also the German Labour Protection Act.
[768] Commercial Code, art. 225-102-5, inserted by the Vigilance Law.
[769] Articles 1240 and 1241 of the French Civil Code.
[770] Commercial Code, article L. 225-102-4.-II, inserted by the Vigilance Law.
[771] French Constitutional Court, Decision No 2017-750 DC, para. 27.
[772] Article 1(d), The Netherlands Child Labour Due Diligence Act.
[773] *Ibid* at article 7(1)-7(3).

possible exclusion of the company from public procurement until such time as the company has proved its reliability,[774] the latter of which is also found in Spanish law.[775]

However, as the focus of The Netherlands Child Labour Due Diligence Act is on the protection of Dutch consumers and not on the victims of child labour, it does not contain provisions relating to access to remedy for the actual victims of child labour, so any remedy in that regard would be dependent on general Dutch tort law. The claimants under Dutch tort law, nevertheless, would still be able to rely indirectly on the Act if the violation of the Act by the company could be construed as an indication of an act contrary to a duty of care to society.[776] More broadly, there have been cases before Dutch courts for parent company liability for abuses of human rights and environmental damage, which have been successful where it has been shown that there was the necessary degree of control by the parent company over the subsidiary.[777] There are similar general tort provisions and case law in Italy.[778] In contrast, the proposed German Legislation on Corporate Human Rights and Environmental Due Diligence in Global Value Chains provides more assistance for victims in that companies are obliged to waive the statute of limitations for any claim completion of the required corporate non-judicial grievance procedure.[779]

Under both The Netherlands Child Labour Due Diligence Act and the proposed German Legislation on Corporate Human Rights and Environmental Due Diligence in Global Value Chains, there is provision for personal criminal liability for the "compliance officer".[780] As with money laundering legislation, companies have to appoint a compliance officer who monitors compliance with the due diligence obligations and must be able to exercise their tasks in a competent and independent way (such as having high level links to management). Where the compliance officer breaches their obligations, such as by a violation of the implementation of a due diligence process that causes serious bodily harm, the compliance officer themselves incur personal criminal liability. This can be punishment of a maximum of 2 years' imprisonment and a €20,500 fine.[781]

In a range of other areas of national law there are specific enforcement regimes. For example, the Italian enforcement provisions under the Italian Consumer Code do allow for enforceability of corporate codes of conduct, on the basis that lack of compliance by a professional with the standards set forth pursuant to their code of conduct shall be considered as misleading advertising, if the commitment can be ascertained and considered to be binding in accordance with the professional usages. If this condition is met, consumers can claim that there is a lack of respect of the code of conduct or file a collective civil action.[782] This could mean that the ability to bring an action applies where the company defines its product as ethical or as complying with human rights protection, and human rights abuses occur down the supply chain including beyond the first tier. It is also of note that, in a case involving ILVA, the biggest steel company in Italy, the Italian courts recognized the right of victims to become a civil party and claim compensation for environmental damages, and ordered the seizure of the plants blast

[774] Article 16 proposed German Legislation on Corporate Human Rights and Environmental Due Diligence in Global Value Chains.
[775] Article 56, Spain's Law on Environmental Assessment.
[776] See Liesbeth Enneking, *Foreign Direct Liability and Beyond – Exploring the Role of Tort Law in Promoting International Corporate Social Responsibility and Accountability* (Eleven International Publishing 2012).
[777] See for example, Dutch Supreme Court, 11 September 2009, JOR 2009, 309 (*Comsys*).
[778] See, for example, the civil proceeding by Timi (as representative of the Nigerian Ikebiri community) of human rights and environmental claims against ENI (the Italian State-owned energy company) and NAOC (its Nigerian subsidiary) currently pending before the Tribunal of Milan.
[779] Article 9 VI, proposed German Legislation on Corporate Human Rights and Environmental Due Diligence in Global Value Chains.
[780] Article 9 The Netherlands Child Labour Due Diligence Act and Article 14 proposed German Legislation on Corporate Human Rights and Environmental Due Diligence in Global Value Chains.
[781] Article 9, The Netherlands Child Labour Due Diligence Act.
[782] See A. Bonfanti, Corporate Social Responsibility and Corporate Accountability: The Italian Private International Law Perspective (2012).

furnaces.[783] In Spain, the law on private security allows for imposition of fines, termination of licences and a ban on directors holding directorships in the sector.[784] Further, according to the Spanish Supreme Court, when an accident at workplace occurs, the liability of the employer arises if the defendant company has not taken general or specific prevention measures, and an effective link exists between the injury and the action or omission.[785] Under German law, a fine can be imposed on the business entity itself if its director commits an offence that violates duties incumbent upon the company or that leads to an unjustified enrichment of the company.[786] For example, after the Volkswagen exhaust emissions scandal in 2018, a public prosecutor imposed a fine on the company for breach of its supervisory duties in ensuring compliance with the German regulation implementing Framework Directive 2007/46/EC on the approval of motor vehicles.[787]

Interestingly, the National Contact Points have, to a large extent, not been very active in monitoring compliance and enabling remedies for victims in this specific area across the Member States surveyed. There are only a few exceptions in the Member States surveyed where there have been cases in this area which have been considered on their merits.[788]

While there are a variety of monitoring means (including private and public) and enforcement processes (through both specific legislation and general tort law) across the Member States surveyed, there are generally remedies available for breaches by companies of their obligations of due diligence in human rights and environmental matters. These remedies are not always to the victims,[789] as fines go to the States and not directly to victims, and the process is not always easy for victims or stakeholders to bring claims. Interestingly, the more recent specific laws and proposals on due diligence include a criminal penalty for company officers if they do not comply with these laws.

4.3.8 Conclusions

It is, therefore, very clear that human rights and environmental due diligence is a practice and process that is applied in many and diverse laws across Member States, and is not at all unfamiliar in these national laws. While the terminology may vary, the same aim of having a legal obligation on a company to create and apply a human rights and environmental impact assessment to consider the risk to stakeholders is found in these Member States. Hence, a use of the term "due diligence" in relation to human rights and the environment in any EU legislation would not appear to be a problem for harmonisation within the Member States surveyed.

The detailed examination here of the laws on due diligence for human rights and environmental issues of 12 Member States with a diversity of legal systems and approaches also indicates that there are legal obligations on companies in this area. These laws generally extend to all listed private companies of a certain size (in terms of employees or turnover), and normally for all relevant national and international human rights and environmental law. There are also many examples of considerably broader scope found in national law, including application to the public sector. In addition, there are a considerable number of national laws which apply the due diligence obligations to

[783] See HRIC et al, *The Environmental Disaster and Human Rights violations of the ILVA steel plant in Italy* (2018).
[784] Spanish Law on Private Security.
[785] See Spanish Supreme Court, STS de 2 de octubre de 2000; STS 26 de marzo de 1999.
[786] Article 130, 30 German Administrative Offences Act.
[787] See https://freeamericanetwork.com/vw-fined-one-billion-euros-by-german-prosecutors-over-emissions-cheating.
[788] See Danish National Contact Point for the OECD, Specific instance on the Danish NCP's own instigation: The due diligence process of the Danish Ministry of Defence in regard to the contracting and building of the inspection vessel Lauge Koch statement (September 6, 2018) and the German National Contact Point: https://www.bmwi.de/Redaktion/EN/Textsammlungen/Foreign-Trade/national-contact-point-ncp.html.
[789] See UNGPs, Commentary to Guiding Principle 25.

all companies domiciled in that State (being based on EU law in this regard) and, in some instances, to other companies.

Further, there is usually an extension of the obligations to subsidiaries of companies, wherever they are domiciled, and an increasing number of laws which specifically include suppliers as part of the company's obligations to act with due diligence in human rights and environmental matters. The independent review in Ireland of its provision in this area, summarises this development:[790]

> [H]uman rights due diligence ought to be considered as a minimum requirement for State companies, businesses that obtain government contracts through the public procurement process, businesses that Ireland engages with through its embassies and State agencies and bodies that derive State support and that act outside the jurisdiction. Human rights due diligence should include reporting on human rights practices outside the jurisdiction so that companies that provide human rights reporting in Ireland, whether due to being domiciled in Ireland, or otherwise, must also report on the human rights of their out of territory operations.

This is a useful summary of the reasons for having mandatory human rights and environmental due diligence, and including within it requirements in public procurement and export credit. In addition, there are some form of enforcement measures and remedies available in most Member States for breaches of these obligations.

The developments in mandatory due diligence for human rights and environmental impacts on companies in the EU can be seen in the recent specific laws on due diligence in human rights and environmental matters in France, The Netherlands, and the United Kingdom. There are also proposed laws, which have been drafted in full in Germany, or not yet fully formulated in Belgium,[791] Denmark, [792] and Finland.[793] These show an increasing expectation of human rights and environmental due diligence obligations on companies in the EU. In addition, many of these laws and proposed laws have support from companies, as they wish to have legal certainty,[794] which any EU wide regulation would enhance.

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[790] ReganStein et al, *National Plan on Business and Human Rights; Baseline Assessment of* Legislative and Regulatory Framework, March 2019, p. 20 *available at*: https://www.dfa.ie/media/dfa/ourrolepolicies/humanrights/Baseline-Study-Business-and-Human-Rights-v2.pdf at p.22.
[791] See https://bit.ly/2YgzpkX.
[792] See Fremsat den 24. januar 2019 af Rasmus Nordqvist (ALT), Eva Flyvholm (EL) og Lisbeth Bech Poulsen (SF) Forslag til folketingsbeslutning om at gøre det lovpligtigt for virksomheder at udøve nødvendig omhu på menneskerettighedsområdet og om indførelse af effektive retsmidler, Beslutningsforslag nr. B 82 (January 24, 2019).
[793] See Ykkösketjuun official website https://ykkosketjuun.fi/en/.
[794] See Robert McCorquodale, Lise Smit, Stuart Neely and Robin Brooks "Human Rights Due Diligence in Law and Practice: Good Practices and Challenges of Business Enterprises" (2017) 2 *Business and Human Rights Journal* 195.

IV. PROBLEM ANALYSIS AND OPTIONS FOR REGULATORY INTERVENTION

1. Introduction

This section sets out the problem analysis, policy background and intervention logic, and develops a set of regulatory options in accordance with Task 3 of the TOR. The framework used is that of the EU Better Regulation guidelines and toolbox.[795]

2. Problem analysis

This section defines the relevant problems and their drivers.

2.1 Adverse human rights and environmental impacts in global value chains, aggravated by their increasingly complex, dynamic and non-transparent character

Human rights and environmental harms related to business operations are well-documented both within and outside of the EU.[796] This situation is aggravated as a result of globalisation, which has led to increasingly complex, dynamic and non-transparent global supply and value chains.[797]

Adverse impacts can take place within all sectors, and have impacts on all human rights and the environment. The following examples, some of which are considered to be common or even widespread, demonstrate the wide range of human rights and environmental impacts allegedly caused or contributed to by or linked to the operations of businesses (including European companies) that have been documented by civil society, international organisations, courts, scientists and other sources:[798]

- Global temperatures and extreme weather conditions are increasing,[799] leading to calls by the United Nations for the international community, states and businesses to take action together.[800]
- The size of the EU's environmental footprint,[801] insofar as "Europe is currently living on emission and resource credits provided by other parts of the world".[802]
- The contribution to climate change through particularly high greenhouse gases emitted by companies in the energy sector.[803] In particular, it has been shown

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[795]Available at: https://ec.europa.eu/info/law/law-making-process/planning-and-proposing-law/better-regulation-why-and-how/better-regulation-guidelines-and-toolbox_en.

[796] See for example the extensive resources collected by the Business and Human Rights Resource Centre, available at: www.business-humanrights.org.

[797] Horatia Muir-Watt, "Private International Law Beyond the Schism" (2011) 2 *Transnational Legal Theory* 347.

[798] These examples were selected as a sample, and are not exhaustive of the types of impacts that can occur due to business operation. While the examples focus on adverse impacts of EU companies, similar problems have been documented for the globalised supply and value chains of non-EU companies.

[799] World Meteorological Organization, "WMO Statement on the State of the Global Climate in 2018" (March 2019), available at: https://gallery.mailchimp.com/daf3c1527c528609c379f3c08/files/82234023-0318-408a-9905-5f84bbb04eee/Climate_Statement_2018.pdf.

[800] "New UN Global Climate report 'another strong wake-up call' over global warming: Guterres", *UN News* (28 March 2019), available at: https://news.un.org/en/story/2019/03/1035681.

[801] Joanne Scott, "Reducing the EU's Environmental Footprint Through 'Territorial Extension'" in V. Mauerhofer, D. Rupino & L. Tarquinio (eds.), *Sustainability and Law* (forthcoming, Springer, 2019).

[802] Arnold Tukker, Tanya Bulavskaya, Stefan Giljum, Arjan de Koning, Stephan Lutter, Moana Simas, Konstantin Stadler, Richard Wood "Environmental and resource footprints in global context: Europe's structural deficit in resource endowments" (2016) 40 *Global Environmental Change* 171 at 179.

[803] For instance, German company RWE, was accused of contributing to climate change, as one of the world's top emitters of greenhouse gases, and asked by a Peruvian farmer in 2015 to contribute its share (proportional to its historic CO2 emissions) to the cost of protecting his house and the village of Huaraz from the risk of flooding due to the melting of two

that 100 major companies are responsible for over 70% of greenhouse gas emissions.[804]

- Deforestation in global supply chains, and large-scale imports of deforestation goods into the EU.[805]
- The decline of ecosystems and biodiversity which is accelerating at unprecedented rates, and has been recognised by the UN Environment as posing risks for "economies, livelihoods, food security, health and quality of life worldwide".[806]
- Low wages not satisfying the basic needs of workers and their families in the garment sector.[807]
- Pollution of the environment resulting in the loss of livelihoods and health for local communities as the result of the activities of the subsidiaries of multinational companies,[808] or the disposal of industrial waste in developing countries without adequate treatment by subcontractors of multinational companies in the mining and energy sectors.[809]
- Fatalities and injuries suffered as a result of unsafe working conditions in factories in the garment sector supply chain.[810]

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glaciers into a lake. On this case, see BHRRC, "RWE lawsuit (re climate change)", available at: https://www.business-humanrights.org/en/rwe-lawsuit-re-climate-change.

[804] BHRRC, "Turning up the Heat: Corporate Legal Accountability for Climate Change", *Corporate Legal Accountability Annual Briefing 2018*, available at: https://www.business-humanrights.org/sites/default/files/CLA_AB_2018_Full.pdf at 5. See also Bryan Cave Leighton Paisner "Addressing Climate Change in Due Diligence for Corporate Transactions" (9 January 2019), available at: https://www.jdsupra.com/legalnews/addressing-climate-change-in-due-93555/.

[805] Fern, "Stolen Goods: The EU's Complicity in Illegal Tropical Deforestation", (March 2015), available at: https://www.fern.org/fileadmin/uploads/fern/Documents/Stolen%20Goods_EN_0.pdf.

[806] Intergovernmental Science-Policy Platform on Biodiversity and Ecosystem Services (IPBES), "Nature's Dangerous Decline 'Unprecedented' Species Extinction Rates 'Accelerating'", Press Release (6 May 2019), available on UN Environment website at: https://www.unenvironment.org/news-and-stories/press-release/natures-dangerous-decline-unprecedented-species-extinction-rates.

[807] Fair Wear Foundation, "Using Due Diligence in Labour Costing to Meet Wage Compliance" (2018), available at: https://api.fairwear.org/wp-content/uploads/2018/11/FWF-Due_Diligence-paper-2018-DEF-digital.pdf.

[808] Examples include the oil spills arising out of the activities of the Nigerian subsidiary of Anglo-Dutch company Shell in the Niger Delta which reportedly affected the health and livelihood of the communities living in the surrounding areas. On this case see Amnesty International "Negligence in the Niger Delta: Decoding Shell and Eni's Poor Record on Oil Spills" (2018), available at: https://www.amnesty.org/download/Documents/AFR4479702018ENGLISH.PDF. Another example can be provided by English company BP which was accused of causing environmental damage to the land of Colombian farmers (including cutting across key water sources which caused soil erosion and spoiled crops and fish ponds) as a result of the construction of an oil pipeline by a consortium led by BP. On this case, see BHRRC, "BP lawsuit (re Colombia)", available at: https://www.business-humanrights.org/en/bp-lawsuit-re-colombia?page=1.

[809] For example, in August and September 2006, the English company Trafigura Ltd. (subsidiary of the Dutch company Trafigura Beheer BV) arranged for the offloading of industrial waste from the Probo Koala ship that it had chartered and the disposal of such waste in Côte d'Ivoire by a local contractor through its Ivorian subsidiary. The waste was disposed of without appropriate treatment by the latter in various sites around the city following which over 100,000 residents were reported to have sought medical assistance. On this case, see Okechuku Ibeanu, "Report of the Special Rapporteur on the adverse effects of the movement and dumping of toxic and dangerous products and wastes on the enjoyment of human rights , Mission to Côte d'Ivoire (4 to 8 August 2008) and the Netherlands (26 to 28 November 2008)", A/HRC/12/26/Add.2 (3 September 2009), available at: https://www2.ohchr.org/english/bodies/hrcouncil/docs/12session/A-HRC-12-26-Add2.pdf. Another example concerns the Swedish mining company Boliden which exported industrial waste (smelter sludge) to Chile where it was disposed of by a subcontractor of the company without being adequately processed, allegedly causing local communities to suffer from health issues as well as adverse environmental impacts. On this case, see BHRRC, "Boliden lawsuit (re Chile)", available at: https://www.business-humanrights.org/en/boliden-lawsuit-re-chile.

[810] For example, the collapse of the Rana Plaza Building in Bangladesh on 24 April 2013 caused the deaths of 1,138 workers and left more than 2,500 others injured. The eight-story building notably housed garment factories. European brands that were sourcing from these garment factories included Primark (UK/Ireland), Mango (Spain), Carrefour (France), Benetton (Italy), El Corte Ingles (Spain), Bon Marche (UK), Kik (Germany) and Matalan (UK). Large structural cracks had been discovered in the building the day before the collapse and prompted an evacuation. However, garment workers were ordered to return to work the following day when the building collapsed. On this case, see Clean Clothes Campaign, "Rana Plaza: a man-made disaster that shook the world", available at: https://asia.floorwage.org/ua/2013/rana-plaza. Just a few months earlier, on 11 September 2012, a fire erupted in the Ali Enterprises textile factory in Pakistan causing the death of 258 workers and leaving dozens more injured. German clothing retailer KiK was the factory's main customer. KiK had established its own Supplier Code of Conduct requiring its worldwide suppliers to comply with certain standards. In addition, a few weeks before the fire, the factory had been awarded the SA8000 certification (meant to ensure compliance with global standards, notably with regard to health and safety) by Italian auditing company RINA who itself subcontracted the inspection to a Pakistani company. However, a computer simulation of the fire textile factory put together by Forensic Architecture at Goldsmiths (University of London) at the request of the ECCHR showed that inadequate fire safety measures, such as the lack of stairs, emergency exits, fire extinguishers and fire alarms in the factory, contributed to the death and injury of hundreds of factory workers. The simulation demonstrated that minor improvements to the safety measures in place - in particular, accessible stairways and clearly signposted escape routes - would have significantly altered the progression of the fire and spared many lives. LG Dortmund, Urteil vom 10.01.2019 - 7 O 95/15, available at: https://openjur.de/u/2155292.html (first instance); OLG Hamm, Beschluss vom 21.05.2019 - 9 U 44/19, available at: https://openjur.de/u/2174526.html (second instance). On this case, see ECCHR, "Kik: Paying the price for clothing production in South Asia", available at: https://www.ecchr.eu/en/case/kik-

- The removal of indigenous communities from their land without free, prior and informed consent for the purposes of projects financed by multinational investors.[811]
- Torture, killings of individuals[812] by security services enlisted by companies to assist the resolution of a dispute surrounding the business activities in particular in the forestry and mining sectors.
- Torture and killing of human rights defenders,[813] "in 2017 [...] 201 land and environmental defenders were killed and many more were attacked, threatened or criminalised for speaking out for their communities, their way of life and the environment. [...] Forty defenders were killed protesting against agribusiness companies, including for palm oil, coffee, tropical fruit, sugar cane and cattle ranching".[814]`
- Attempts at silencing human rights defenders through Strategic Lawsuits Against Public Participation (SLAPPs). For instance, the Business and Human Rights Resource Centre found that 12 carbon majors brought at least 24 lawsuits against 71 environmental and human rights defenders between 2015 and 2015, for a total of US$ 904 million in damages.[815]
- Unlawful detentions and killings of individuals after their private information was obtained from telecommunications companies, or through the surveillance equipment provided by them.[816]
- Hate crimes and genocide encouraged by hate speech and harmful online content on the platforms of private internet companies.[817]

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paying-the-price-for-clothing-production-in-south-asia/. Other similar incidents include the textile factory fire in the Tazreen factory in Bangladesh on 24 November 2012 which caused the death of 112 workers who were producing clothes notably for European brands such as El Corte Ingles (Spain), C&A (Belgium/Germany) and KiK (Germany). On this case, see Clean Clothes Campaign, "Six years after deadly garment factory fire, Bangladesh risks new wave of factory incidents", available at: https://cleanclothes.org/news/2018/11/24/tazreen-fashions-6-years.

[811] On these issues, see Yorck Diergarten, "Indigenous or Out of Scope? Large-scale Land Acquisitions in Developing Countries, International Human Rights Law and the Current Deficiencies in Land Rights Protection" (2019) 19:1 *Human Rights Law Review* 37.

[812] For instance, German-owned logging business Danzer allegedly aided and abetted gross human rights violations carried out by the police and military forces (through providing financial and logistical assistance) against a forest community in the Democratic Republic of the Congo on 2 May 2011, which included sustained beatings of the villagers, rape, arbitrary arrest and destruction of property. On this case, see Greenpeace, "Stolen future: Conflicts and logging in Congo's rainforests - the case of Danzer", available at: https://www.greenpeace.org/archive-international/Global/international/publications/forests/2011/stolen%20future.pdf. Other examples include the English company African Minerals accused of complicity in human rights abuses carried out by the police forces in Sierra Leone to quell villagers' protests against the company's mining operations in 2010 and 2012, which included assault, false imprisonment, rape and murder. On this case, see BHRRC, "Tonkolili Iron Ore lawsuit (re complicity in violence against villagers in Sierra Leone)", available at: https://www.business-humanrights.org/en/tonkolili-iron-ore-lawsuit-re-complicity-in-violence-against-villagers-in-sierra-leone. In 2008, Tanzanian villagers were killed and injured by police and security forces at the North Mara Mine owned by the Tanzanian subsidiary of the English company Acacia Mining (formerly African Barrick Gold). Both companies were accused of being complicit in the human rights abuses and failing to prevent the use of excessive force by the security and police forces at the mine. On this case, see BHHRC, "African Barrick Gold lawsuit (re Tanzania)", available at: https://www.business-humanrights.org/en/african-barrick-gold-lawsuit-re-tanzania. In May 2012, a number of Peruvian citizens were severely injured and two persons were killed by the Peruvian National Police (PNP) in the course of an environmental protest at the Tintaya copper mine then owned by the Peruvian subsidiary of the English company Xstrata, both of which allegedly provided logistical assistance to PNP. On this case, see BHRRC, "UK High Court to hear claim over Glencore's liability for alleged killings and injuries of protestors at Tintaya mine", available at: https://www.business-humanrights.org/en/uk-high-court-to-hear-claim-over-glencore's-liability-for-alleged-killings-injuries-of-protestors-by-peruvian-police-at-tintaya-copper-mine#c164399.

[813] This is increasingly such a widespread issue that the Business and Human Rights Resource Centre has an entire portal dedicated to track and document examples of attacks on human rights defenders in the context of business activity: https://www.business-humanrights.org/en/bizhrds. To date, last visited 27 October 2019, the number of attacks tracked in the portal stand at 1983. The portal further indicates that "[o]ver 1400 attacks on defenders working on businesses-related human rights abuses took place from 2015-2018".

[814] ClientEarth and Global Witness, "Strengthening Corporate Responsibility: The case for mandatory due diligence in the EU to protect people and the planet" (July 2019), available at: https://www.globalwitness.org/en/campaigns/forests/strengthening-corporate-responsibility/.

[815] BHRRC, "Silencing the Critics: How big polluters try to paralyse environmental and human rights advocacy through the courts", (30 September 2019), available at: https://www.business-humanrights.org/en/silencing-the-critics-how-big-polluters-try-to-paralyse-environmental-and-human-rights-advocacy-through-the-courts.

[816] For instance, French company Amesys allegedly provided surveillance equipment to the Gaddafi regime in Libya which was used to intercept private internet communications, and to identify dissidents who were then arrested and tortured. On this case, see FIDH, "The Amesys Case", available at: https://www.fidh.org/IMG/pdf/report_amesys_case_eng.pdf. Another example involves the French company Qosmos which allegedly provided surveillance equipment to the Bashar Al Assad government in Syria used to identify, arrest and torture dissidents. On this case, see BHRRC, "Qosmos investigation (re Syria)", available at: https://www.business-humanrights.org/en/qosmos-investigation-re-syria.

- Modern slavery, forced labour and human trafficking in the supply chains of consumers goods that are sold at European supermarkets.[818]
- Exploitation of migrant workers in construction sites operated by the subsidiaries of multinational companies.[819]
- Genocide, war crimes and crimes against humanity by governments or terrorist enterprises financed by multinational companies or investors.[820]
- Widespread use of child labour in cocoa farms in Côte d'Ivoire and Ghana to produce goods, including chocolate, for the European market.[821]
- Torture, violence, rape and killings of individuals in conflict zones fuelled by sourcing of certain minerals by multinational companies to make products including laptops, mobile phones and cars sold on the European market.[822]

These examples, which do not constitute an exhaustive list, arise both in companies' own operations and within their global value chains. Supply chains of transnational companies often have tens of thousands of suppliers across multiple tiers. Companies often only have direct contractual relationships with first tier suppliers, and very limited or no visibility of the supply chain beyond that. First tier suppliers are often protective of information with respect to their further supply chain.[823] Leverage over suppliers differs vastly depending on the size of the company, the size of the suppliers, and the nature of the relationship.[824]

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[817] Examples of this include the role of the Internet and social media platforms having enabled the spread of hateful and divisive rhetoric in Myanmar, see UN Human Rights Council, "Report on the detailed findings of the Independent International Fact-Finding Mission on Myanmar", A/HRC/39/CRP.2 (17 September 2018).

[818] A 2017 BHRRC report noted that modern slavery is prevalent "in almost every global supply chain". BHRRC, "Modern Slavery in Company Operation and Supply Chains: Mandatory transparency, mandatory due diligence and public procurement due diligence" (September 2017), available at: https://www.business-humanrights.org/sites/default/files/documents/Modern%2520slavery%2520in%2520company%2520operation%2520and%2520supply%2520chain_FINAL.pdf at 2. Examples include the forced labour, human trafficking and other serious gross rights abuses of migrant workers (including children) on the Thai fishing boats producing fishmeal that feeds farmed prawns which are notably purchased by European supermarkets such as Tesco (UK), and Carrefour (France). On this case, see Human Rights Watch, "Hidden Chains: Rights Abuses and Forced Labor in Thailand's Fishing Industry" (23 January 2018), available at: https://www.hrw.org/report/2018/01/23/hidden-chains/rights-abuses-and-forced-labor-thailands-fishing-industry#_ftn2. Other examples within the EU include the severe labour exploitation (including living and working conditions incompatible with human dignity, working long shifts, and being deprived of sleep and toilet breaks) of Lithuanian workers who were allegedly trafficked to the UK in 2008 to work on chicken farms producing eggs purchased by English supermarkets. On this case, see BHRRC, "DJ Houghton lawsuit (re trafficked Lithuanian migrants)", available at: https://www.business-humanrights.org/en/dj-houghton-lawsuit-re-trafficked-lithuanian-migrants.

[819] For instance, Irish company Mercury MENA and French company Vinci allegedly violated the human rights of migrant workers involved in their construction sites for the 2022 football World Cup in Qatar. Alleged violations include forced labour, enslavement, reckless endangerment of workers' lives and working conditions incompatible with human dignity. On this case, see Amnesty International, "Unpaid and abandoned: the abuse of Mercury MENA workers" (2018), available at: https://www.amnesty.org/en/latest/research/2018/09/mercury-mena-abuses-qatar/. See also BHRRC, "Vinci lawsuits (re forced labour in Qatar)", available at: https://www.business-humanrights.org/en/vinci-lawsuit-re-forced-labour-in-qatar.

[820] For example, in 1994, French bank BNP Paribas allowed a financial transaction which allegedly participated to financing the purchase of 80 tons of weapons by the Rwandan government which were used to kill over 800,000 people (mostly of the Tutsi minority) during the Rwandan genocide. On this case, see BHRRC, "NGOs file lawsuit in France against BNP Paribas over alleged complicity in genocide in Rwanda", available at: https://www.business-humanrights.org/en/ngos-file-lawsuit-in-france-against-bnp-paribas-over-alleged-complicity-in-genocide-in-rwanda. More recently, 11 former Syrian employees of French company Lafarge and two NGOs filed a criminal complaint against the company for complicity in war crimes and crimes against humanity, deliberate endangerment of people's lives, working conditions incompatible with human dignity, and exploitative and forced labour. Lafarge and its Syrian subsidiary allegedly bought raw material from diverse jihadist groups (including ISIS) and negotiated safe passage for its workers and products in exchange for financial compensations which amounted to approximately 13 million euros. On this case, see BHRRC, "Lafarge lawsuit (re complicity in crimes against humanity in Syria)", available at: https://www.business-humanrights.org/en/lafarge-lawsuit-re-complicity-in-crimes-against-humanity-in-syria.

[821] According to Unicef, "the number of children in hazardous work in cocoa production continues to be a concern" despite the efforts that have been made over the past few years: https://www.unicef.org/csr/cocoa.html.

[822] See for instance SOMO, "Multinational corporations in conflict-affected areas: Risks and challenges around human rights and conflict" (December 2015), available at: https://www.somo.nl/wp-content/uploads/2016/01/Risks-and-challenges-around-human-rights-and-conflict.pdf. See also John Prendergast, "Can you hear Congo now? Cell Phones, Conflict Minerals and the Worst Sexual Violence in the World" (April 2009), available at: https://enoughproject.org/files/Can%20Your%20Hear%20Congo%20Now.pdf.

[823] Robert McCorquodale, Lise Smit, Stuard Neely and Robin Brooks, "Human Rights Due Diligence in Law and Practice: Good Practices and Challenges for Business Enterprises" (2017) 2:2 Business and Human Rights Journal 195 at 222.

[824] The Commentary to UNGP 19 provides that: "Where the relationship is 'crucial' to the enterprise, ending it raises further challenges. A relationship could be deemed as crucial if it provides a product or service that is essential to the enterprise's business, and for which no reasonable alternative source exists".

Contractual provisions and supply chain codes of conduct remain one of the most frequently used tools for implementing supply chain due diligence,[825] but enforcement of contractual obligations on suppliers' due diligence are problematic,[826] and in any event only available where there is a direct contractual relationship, such as with first tier suppliers.

The UN Working Group on the issue of human rights and transnational corporations and other business enterprises notes, in this respect:[827]

> An apparent gap in current supply chain management is that human rights due diligence tends to be limited to tier-one companies. Efforts to go beyond tier one tend to happen only when the issue has been brought to light by the media or non-governmental organisations (NGOs). Few companies appear to be asking tier-one suppliers to demonstrate that they — and their suppliers in the tiers below — fulfil the responsibility to respect human rights by requiring assessments of the risks to and impacts on human rights.

Traceability of entities and activities in the supply chain is a commonly cited issue, although, increasingly, some companies demonstrate that they have taken steps to increase traceability and map the supply chain. Steps have also been taken to develop human rights audits, using a human rights lens and human rights experts as auditors. However, it is widely acknowledged[828] that audits are limited. In addition, as demonstrated by our survey, very limited practices are currently being utilised for downstream due diligence.

Close cooperation and deep engagement with suppliers are required to ensure meaningful improvement in practices. Other solutions to the supply chain visibility issue can be found in the reduction of complexity of supply chains and exploration of technology such as blockchain.

2.2 Lack of implementation of due diligence by companies, despite existing voluntary and legally binding transparency and reporting requirements

Since the adoption of the UNGPs, various legislative developments and voluntary standards at international, regional, domestic and industry level have introduced due diligence transparency and reporting requirements.[829] These standards are often accompanied by detailed guidance.

However, research has shown that implementation levels of supply chain due diligence requirements are low, despite the increasing presence of transparency and reporting requirements.[830] According to the available data, only a small number of companies take

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[825] Ibid at 215.

[826] Cases like the KiK case have illustrated the limitations of this sort of contractual obligation. Indeed, in spite of the Supplier Code of Conduct established by KiK and requiring its suppliers worldwide to comply with certain standards, including health and safety standards, actual compliance with such standards remained problematic in practice, and inadequate fire safety measures reportedly contributed to the death and injury of many factory workers in the fire that erupted in the textile factory of KiK's supplier in Pakistan. On this case, see Axel Marx, Claire Bright and Jan Wouters, "Access to Legal Remedies for Victims of Corporate Human Rights Abuses in Third Countries" (February 2019), available at: http://www.europarl.europa.eu/RegData/etudes/STUD/2019/603475/EXPO_STU(2019)603475_EN.pdf at 59.

[827] UN Working Group on the issue of human rights and transnational corporations and other business enterprises, A/73/163 (16 July 2018) at para 29.

[828] Marx, Bright and Wouters, above n 826 at 66, which highlights that KiK's textile factory had been audited in order to receive the SA8000 certification which was awarded just three weeks before the fire and in spite of inadequate fire safety measures. Studies have confirmed the limitations of audits. See also Genevieve LeBaron and Jane Lister, "Ethical Audits and the Supply Chains of Global Corporations", *Sheffield Political Economy Research Institute Global Political Economy Brief No. 1* (January 2016), available at: http://speri.dept.shef.ac.uk/wp-content/uploads/2018/11/Global-Brief-1-Ethical-Audits-and-the-Supply-Chains-of-Global-Corporations.pdf. These limitations have been confirmed by interviewees in this study.

[829] For details, see Section 3 Regulatory Review.

[830] For example, see Alliance for Corporate Transparency, "2018 Research Report: The State of Corporate Sustainability Disclosure under the EU Non-Financial Reporting Directive", available at: http://www.allianceforcorporatetransparency.org/assets/2018_Research_Report_Alliance_Corporate_Transparency-

any steps to implement such due diligence. In cases where companies do take some steps, their due diligence processes often fall short of the standards expected.[831]

In a report on the implementation of human rights due diligence the UN Working Group on the issue of human rights and transnational corporations and other business enterprises noted that:[832]

> According to human rights benchmarking and rating assessments, the majority of companies covered by the assessments do not demonstrate practices that meet the requirements set by the Guiding Principles. This may indicate that risks to workers and communities are not being managed adequately in spite of growing awareness and commitments. One of the indicators is the lack of focus on human rights risks in most current reporting, which is at best a result of inadequate communication or at worst a reflection of insufficient understanding and management of risks to human rights. In general, there is much room for improvement regarding transparency on the concrete details of risk assessments and human rights due diligence processes. Often human rights due diligence is not understood properly, resulting in:
>
> (a) Misconstruction of risk, namely, when companies operate with a mindset of risk to the business and not risk to rights holders, such as workers, communities and consumers. Related to that, there is a lack of understanding on how better human rights due diligence will also improve the overall risk management approach. Reluctance or even pushback from traditionally oriented legal counsel, both in-house and external, fearing disclosure is a key obstacle to uptake by companies;
>
> (b) Failure to address the most significant risks to human rights first and focusing instead on risks that may be relatively easy to address or that are getting attention in a given context, such as modern slavery or diversity, rather than doing an objective assessment of the most significant and likely risks to people affected by the activities and business relationships of the enterprise;
>
> (c) Too many human rights impact assessments done as exercises to tick the box, without meaningful engagement with stakeholders, including engagement with vulnerable or at-risk groups and critical voices such as human rights defenders;
>
> (d) Most business enterprises still being mostly reactive, instead of proactively trying to identify potential human rights impacts before they arise, including through early-stage meaningful engagement with potentially affected stakeholders.

66d0af6a05f153119e7cffe6df2f11b094affe9aaf4b13ae14db04e395c54a84.pdf. See discussion below, section 5.3. See also Genevieve LeBaron and Andreas Rühmkorf, "Steering CSR Through Home State Regulation: A Comparison of the Impact of the UK Bribery Act and Modern Slavery Act on Global Supply Chain Governance" (2017) 8:3 *Global Policy* 15; Karin Bhuman, "Neglecting the Proactive Aspect of Human Rights Due Diligence? A Critical Appraisal of the EU's Non-Financial Reporting Directive as a Pillar One Avenue for Promoting Pillar Two Action" (2018) 3:1 *Business and Human Rights Journal* 23. See also PwC, "Strategies for Responsible Business Conduct", Report prepared at the request of the Ministry of Foreign Affairs of the Netherlands (December 2018), available at: https://zoek.officielebekendmakingen.nl/blg-874902.pdf at 59; Business & Human Rights Resource Centre, "FTSE 100 & the UK Modern Slavery Act: From Disclosure to Action", available at: https://www.business-humanrights.org/sites/default/files/FTSE%20100%20Briefing%202018.pdf; Frank Field, Maria Miller and Baroness Butler-Sloss, "Independent Review of the Modern Slavery Act, Second interim report: Transparency in supply chains", available at: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/796500/FINAL_Independent_MSA_Review_Interim_Report_2_-_TISC.pdf.

831 Ibid.

832 UN Working Group on the issue of human rights and transnational corporations and other business enterprises, above n827 at para 25.

The drivers of this low implementation are commonly perceived to be a lack of monitoring and enforcement of the requirements, as well as a failure of current corporate risk assessment processes to extend beyond the materiality of the risks to the company to the severity of the risks to those who are affected by the adverse impacts (see next sub-section). Moreover, existing requirements mainly require reporting, which is only one of the components of due diligence.[833]

Due diligence is defined as a process which includes four broad components:[834]

1. Identifying and assessing actual and potential impacts
2. Integrating and acting upon the findings
3. Tracking the effectiveness of these actions, and
4. Communicating how impacts are addressed, including through reporting.

Regulatory reporting requirements can be legally complied with by simply reporting, without taking any of the other steps of due diligence. As such, reporting requirements do not require substantive due diligence as part of the legal requirement. Very few reporting requirements to date have been accompanied by enforcement provisions for failing to report in accordance with the requirement. Moreover, existing examples of reporting requirements have also not been accompanied by enforcement mechanisms for failure to implement adequate due diligence processes. A recent report prepared at the request of the Dutch Ministry of Foreign Affairs pointed out that these types of reporting requirements rely on the underlying assumption according to which there is no explicit need to push for enforcement as "businesses would be eager to comply due to the pressure they face from civil society, consumers and investors".[835] Another scholar explains that "the reasoning implies that the risk of the possibility of firms being challenged by civil society groups, investors, consumers and stakeholders for their business practices will drive change proactively to avoid reputational damage and reactions by stakeholders like investors or consumers that may have economic impacts on the firm".[836] However, in practice, widespread issues of corporate non-compliance have made this assumption seem questionable.[837] In addition, it has been noted that:[838]

> [W]hen reporting is undertaken with a compliance perspective, the likely result is a report offering a picture that corresponds to stakeholders' ideal image of the firm without generating learning for the organization, nor necessarily sharing information that critical social actors need in order to hold firms to account for their impacts, policies, and reported information.

As a result, many studies have highlighted the lack of concrete impact of these types of regulatory measures,[839] and the fact that they have not delivered in terms of driving actual change in corporate behaviour in practice.[840]

Moreover, the lack of due diligence within companies' own operations and supply chains is frequently a result of internal incoherence within companies, particularly around

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[833] Chiara Macchi and Claire Bright, "Hardening Soft Law: The Implementation of Human Rights Due Diligence Requirements in Domestic Legislation" in M. Buscemi, N. Lazzerini and L. Magi, *Legal Sources in Business and Human Rights - Evolving Dynamics in International and European Law* (forthcoming, Brill, 2019).
[834] UNGP 17.
[835] PwC, above n 830 at 37.
[836] Bhumann, above n 830 at 28.
[837] NYU Stern Center for Business and Human Rights, "Research Brief: Assessing Legislation on Human Rights in Supply Chains: Varied Designs but Limited Compliance" (19 June 2019), available at: https://bhr.stern.nyu.edu/blogs/2019/6/19/research-brief-assessing-legislation-on-human-rights-in-supply-chains at 4.
[838] Bhumann, above n 830 at 37.
[839] See for instance, Frank Field, Maria Miller and Baroness Butler-Sloss, "Independent Review of the Modern Slavery Act 2015 - Final Report" (2019), available at: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/803406/Independent_review_of_the_Modern_Slavery_Act_-_final_report.pdf.
[840] Sandra Cossart, Jérôme Chaplier and Tiphaine Beau de Loménie, "The French Law on Duty of Care: a Historic Step Towards Making Globalization Work for All" (2017) 2:2 *Business and Human Rights Journal* 317 at 319.

buying practices. Even where contractual clauses or supply codes of conduct require human rights and environmental standards, the prices paid to suppliers may not take into account the costs of adhering to these human rights or environmental standards.[841] Often, prices are so low that they do not allow suppliers to pay their workers the local minimum wage[842] or social welfare payments, and delivery times lead to unreasonable working hours. Where the company's due diligence takes place through human rights training and audits, suppliers are often required to pay for such training and audits, with no corresponding increase in the purchase price.[843] For example, Oxfam's 2019 "Supermarket Scorecard" analysing 16 EU and US supermarkets' policies and practices on human rights in their supply chains, identified "unfair trading practices" as one area of priority for action.[844] The report notes that:[845]

> Supermarkets use a range of practices that pressure suppliers - squeezing their ability to pay workers a living wage. Low-price policies in particular contribute to the exploitation of workers. This undermines any good efforts companies place in other areas. Only three supermarkets have committed to eliminate these practices, but no meaningful actions have been disclosed.

2.3 Failure of corporate risk assessment processes to extend beyond the risks of the company to those who are actually or potentially affected by its supply and value chain

Current corporate risk assessment processes are not focused on risks to those who are actually or potentially affected by its operations, supply chain or value chain. In many cases, affected persons (or "rights-holders")[846] are external parties with no relationships to the company.

Traditional reporting on risks and internal risk management processes of companies tend to focus on the risks to the company rather than the risks to those external rights-holders which are actually or potentially affected. Risks are assessed based on materiality of the risks to the company, instead of the severity of the risks to those affected. Even severe harms to those affected may not necessarily pose material risks to the company, whether in the short, medium or long term.

This continues to be the case despite guidance which clarifies that the relevant risks for due diligence must extend beyond the risks of the company to those who are affected (the rights-holders), such as in the UNGPs,[847] the OECD Guidelines,[848] and the EU Commissions' non-binding guidelines on non-financial reporting.[849]

The 2018 report of the United Nations High Commissioner for Human Rights on improving accountability and access to remedy for victims of business-related human rights abuse clarifies in this respect that:[850]

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[841] The Joint Ethical Trading Initiatives, "Guide to Buying Responsibly" (7 September 2017), available at: https://www.ethicaltrade.org/resources/guide-to-buying-responsibly.
[842] Fair Wear Foundation, above n807.
[843] Ibid.
[844] Oxfam, "Supermarkets Scorecard", available at: https://www.oxfam.org/en/behindtheprice/scorecard.
[845] Oxfam, "What are supermarkets doing to tackle human suffering in their supply chains" (3 July 2019), available at: https://views-voices.oxfam.org.uk/2019/07/supermarkets-supply-chains/.
[846] Commentary to UNGP 17.
[847] Ibid.
[848] OECD, "Guidelines for Multinational Enterprises" (2011), available at: http://www.oecd.org/daf/inv/mne/48004323.pdf.
[849] The EU Commission's non-binding guidelines for non-financial reporting expect companies to disclose "relevant information on the actual and potential impacts of its operations on the environment" (4.6a), "material information on social and employee matters" (4.6b), "material information on potential and actual impacts of their operations on right-holders" (4.6c) and so forth. Communication from the Commission, "Guidelines on non-financial reporting (methodology for reporting non-financial information)" (2017/C 215/01), available at: https://ec.europa.eu/info/publications/170626-non-financial-reporting-guidelines_en.
[850] UN Human Rights Council, "Improving accountability and access to remedy for victims of business-related human rights abuse: The relevance of human rights due diligence to determinations of corporate liability", A/HRC/38/20/Add.2 (1 June 2018) at para 8.

Human rights due diligence should not be confused with other forms of legal due diligence activities, such as those carried out in preparation for corporate mergers and acquisitions, or those required for compliance monitoring purposes in areas such as banking or anti-corruption. The key difference between these concepts is that the latter group is generally concerned with identifying, preventing, and mitigating risks to *business*; whereas human rights due diligence is concerned with risks to *people*, specifically from adverse human rights impacts that a business enterprise may cause or contribute to through its own activities, or which may be directly linked to its operations, products, or services by its business relationships. As such, human rights due diligence demands methodologies that are informed, in scope and procedural terms, by internationally recogniszed human rights standards, and should "[i]nvolve meaningful consultation with potentially affected groups and other relevant stakeholders."

2.4 Regulatory gap between existing legal framework and Member States' obligations

The EU and its individual Member States have various international and EU-level legal obligations and commitments for human rights and the environment. Examples include:

- International human rights treaties such as:
    - The Universal Declaration of Human Rights
    - The International Covenant on Civil and Political Rights
    - The International Covenant on Economic, Social and Cultural
    - Rights
    - The principles concerning fundamental rights in the eight ILO core conventions
    - The Declaration on Fundamental Principles and Rights at Work
    - The International Convention on the Elimination of All Forms of Racial Discrimination
    - The Convention on the Elimination of All Forms of Discrimination against Women
    - The Convention against Torture and Other Cruel, Inhuman or Degrading Treatment or Punishment
    - The United Nations Convention on the Right of the Child
    - The International Convention on the Protection of the Rights of All Migrant Workers and Members of Their Families
    - The Convention on the Rights of Persons with Disabilities
    - The International Convention for the Protection of All Persons from Enforced Disappearance
    - The United Nations Declaration on the Rights of Indigenous People
    - The Convention for the Protection of Human Rights and Fundamental Freedoms ("European Convention on Human Rights")
- The Charter of Fundamental Human Rights of the European Union
- The UN Guiding Principles on Business and Human Rights [851]
- The Paris Agreement on climate change
- The UN 2030 Agenda for Sustainable Development of 2015
- The ILO Tripartite declaration of principles concerning multinational enterprises and social policy ("MNE Declaration") of March 2017

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[851] In its 2011 Communication on Corporate Social Responsibility, the European Commission affirmed that: "Better implementation of the UN Guiding Principles will contribute to EU objectives regarding specific human rights issues and core labour standards, including child labour, forced prison labour, human trafficking, gender equality, non-discrimination, freedom of association and the right to collective bargaining." Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, "A renewed strategy 2011-14 for Corporate Social Responsibility", COM(2011) 681 final. See also European Commission, "Commission Staff working document on implementing UNGPs - State of Play", Brussels 16 July 2015, SWD(2015) 144 final at 6.

- The ILO Centenary Declaration for the Future of Work of 2019
- The Beijing Declaration and Platform for Action of 1995
- The Women's Empowerment Principles of 2010

Many of these standards expect Member States to take steps to ensure that people are protected from human rights and environmental harms, including by corporate actors. The UNGPs phrase this international law obligation as follows:

> States must protect against human rights abuse within their territory and/or jurisdiction by third parties, including business enterprises. This requires taking appropriate steps to prevent, investigate, punish and redress such abuse through effective policies, legislation, regulations and adjudication. [852]

These state obligations include the duty to ensure that those affected have access to remedies, as confirmed in UNGP 25:

> As part of their duty to protect against business-related human rights abuse, States must take appropriate steps to ensure, through judicial, administrative, legislative or other appropriate means, that when such abuses occur within their territory and/or jurisdiction those affected have access to effective remedy.

The Commentary to UNGP 25 further confirms:

> Unless States take appropriate steps to investigate, punish and redress business-related human rights abuses when they do occur, the State duty to protect can be rendered weak or even meaningless.

There seems to be a consensus that states are allowed (and some argue, obliged)[853] to regulate the adverse human rights and environmental impacts of their multinational corporations that occur outside their territories. In this respect, John Ruggie, the author of the UNGPs, explained, in a letter he recently wrote as a response to a public letter by Swiss business associations regarding their position on the Swiss Responsible Business Initiative that:[854]

> Guiding Principle 2 provides that states should make clear that the responsibility to respect applies throughout a company's operations. The commentary to Principle 2 goes on to explain that under international human rights law states are not generally required to regulate the extraterritorial activities of businesses domiciled in their jurisdictions, but nor are they generally prohibited from doing so provided that there is a recognized jurisdictional basis. The commentary notes that states have adopted a range of approaches in this regard, specifically

[852] UNGP 1.
[853] Sigrun Skogly, *Beyond National Borders: States' Human Rights Obligations in International Cooperation* (Intersentia, 2004); Robert McCorquodale and Penelope Simons, "Responsibility Beyond Borders: State Responsibility for Extraterritorial Violations by Corporations of International Human Rights Law" (2007) 70: 4 *Modern Law Review* 598; Daniel Augenstein and David Kinley, "When human rights 'responsibilities' become 'duties': the extraterritorial obligations of states that bind corporations" in Surya Deva and David Bilchitz (eds.), *Human Rights Obligations of Business: Beyond the corporate responsibility to respect?* (Cambridge University Press, 2013) 271; Smita Narula, "International financial institutions, transnational corporations and duties of states" in Malcolm Langford, Wouter Vandenhole, Martin Scheinin and Willem van Genugten (eds.), *Global Justice, State Duties. The Extraterritorial Scope of Economic, Social and Cultural Rights in International Law* (Cambridge University Press, 2014) 114; Olivier De Schutter, "Towards a New Treaty on Business and Human Rights" (2016) 1:1 *Business and Human Rights Journal* 41; Sara L. Seck, "Conceptualizing the Home State Duty to Protect" in Karin Buhmann, Lynn Roseberry, Mette Morsing (eds.), *Corporate Social and Human Rights Responsibilities. Global, Legal and Management Perspectives* (Palgrave Macmillan, 2011) 25. Nadia Bernaz, "Enhancing Corporate Accountability for Human Rights Violations: Is Extraterritoriality the Magic Potion?" (2013) 117 *Journal of Business Ethics* 493. See also Claire Methven O'Brien, "The Home State Duty to Regulate the Human Rights Impacts of TNCs Abroad: A Rebuttal" (2018) 3:1 *Business and Human Rights Journal* 47.
[854] BHHRC, "Companies clarify position on Swiss mandatory human rights due diligence initiative", available at: https://www.business-humanrights.org/en/companies-clarify-position-on-swiss-mandatory-human-rights-due-diligence-initiative.

> including domestic legislation that may have extraterritorial effects. In short, extraterritoriality is not per se *ultra vires*.

Olivier De Schutter who has written extensively on the topic, explains that:[855]

> Grounding the exercise of extraterritorial jurisdiction on the principle of active personality would appear to be particularly justified in the case of corporations which have the 'nationality' of the forum State, especially where the prohibitions relate to human rights violations. Indeed, the two justifications traditionally offered for basing extraterritorial jurisdiction on this principle seem to converge in this case. A first justification has been, traditionally, that since nationals traditionally may not be extradited, the extraterritorial application of national legislation on the basis of the principle of active personality ensures that certain crimes would not remain unpunished…Second, by exercising extraterritorial jurisdiction on the basis of the active personality principle, a State ensures that its nationals will not be acting in violation of certain fundamental values abroad, by adopting forms of behaviour which would be considered as offences in the forum State : what the nationals of a State may not do at home, they should not be allowed to do in another State, where the seriousness of the act justifies such an extension of the geographical reach of the prohibition.

Public international law recognises that home States have certain obligations in relation to the regulation of the extraterritorial activities of the companies domiciled on their territory. For example, General Comment No. 16 of the UN Convention on the Rights of the Child provides that:[856]

> Home States also have obligations [...] to respect, protect and fulfil children's rights in the context of businesses' extraterritorial activities and operations, provided that there is a reasonable link between the State and the conduct concerned. A reasonable link exists when a business enterprise has its centre of activity, is registered or domiciled or has its main place of business or substantial business activities in the state concerned.

In addition, Paragraph 30 of the General comment No. 24 on State obligations under the International Covenant on Economic, Social and Cultural Rights in the context of business activities provides that:[857]

> The extraterritorial obligation to protect requires States parties to take steps to prevent and redress infringements of Covenant rights that occur outside their territories due to the activities of business entities over which they can exercise control, especially in cases where the remedies available to victims before the domestic courts of the State where the harm occurs are unavailable or ineffective.

Paragraph 31 adds that:[858]

> This obligation extends to any business entities over which States parties may exercise control, in accordance with the Charter of the United Nations and applicable international law. Consistent with the admissible scope of jurisdiction

[855] Olivier De Schutter, "Extraterritorial Jurisdiction as a tool for improving the Human Rights Accountability of Transnational Corporations", *Faculté de Droit de l'Université Catholique de Louvain* (2006), available at: https://www.business-humanrights.org/sites/default/files/reports-and-materials/Olivier-de-Schutter-report-for-SRSG-re-extraterritorial-jurisdiction-Dec-2006.pdf.
[856] TOR p. 6; General Comment no. 16 on State obligations regarding the impact of the business sector on children's rights.
[857] UN Committee on Economic, Social and Cultural Rights, "General comment No. 24 on State obligations under the International Covenant on Economic, Social and Cultural Rights in the context of business activities", E/C.12/GC/24 (10 August 2017) at para 30.
[858] Ibid para 31.

> under general international law, States may seek to regulate corporations that are domiciled in their territory and/or jurisdiction: this includes corporations incorporated under their laws, or which have their statutory seat, central administration or principal place of business on their national territory. States parties may also utilize incentives short of the direct imposition of obligations, such as provisions in public contracts favouring business entities that have put in place robust and effective human rights due diligence mechanisms, in order to contribute to the protection of economic, social and cultural rights at home and abroad.

Paragraph 33 further states that:[859]

> In discharging their duty to protect, States parties should also require corporations to deploy their best efforts to ensure that entities whose conduct those corporations may influence, such as subsidiaries (including all business entities in which they have invested, whether registered under the State party's laws or under the laws of another State) or business partners (including suppliers, franchisees and subcontractors), respect Covenant rights. Corporations domiciled in the territory and/or jurisdiction of States parties should be required to act with due diligence to identify, prevent and address abuses to Covenant rights by such subsidiaries and business partners, wherever they may be located. The Committee underlines that, although the imposition of such due diligence obligations does have impacts on situations located outside these States' national territories since potential violations of Covenant rights in global supply chains or in multinational groups of companies should be prevented or addressed, this does not imply the exercise of extraterritorial jurisdiction by the States concerned. Appropriate monitoring and accountability procedures must be put in place to ensure effective prevention and enforcement. Such procedures may include imposing a duty on companies to report on their policies and procedures to ensure respect for human rights, and providing effective means of accountability and redress for abuses of Covenant rights.

The current lack of access to remedy for victims of corporate human rights and environment impacts (see subsection below), the absence of an enforceable legal instrument requiring due diligence at EU level, and very few examples of such laws at Member State level, combined with the low levels of implementation of due diligence by companies, suggest a gap between the existing legal framework, and Member States' international and EU human rights and environmental obligations.

2.5 Increasing fragmentation of due diligence requirements across sectors, size of companies, countries, and area of application

There is currently no general legal duty at EU or international level which requires companies to undertake due diligence for human rights and environmental impacts caused by their supply or value chain.

However, since the adoption of the UNGPs in 2011, domestic laws and industry standards have increasingly been introducing due diligence requirements. Although these requirements are based on the UNGPs standard of due diligence, often echoing the UNGPs wording, these existing requirements have not provided uniformity. Instead, they often apply only to certain sectors or issues, and to different categories of companies based on domicile, country of operation or turnover. Multinational companies in

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[859] Ibid para 33.

particular are simultaneously subject to a mosaic of fragmented requirements at domestic and industry level.[860]

The OECD Guidelines expect due diligence to cover all human rights and environmental impacts. Similarly, due diligence in the UNGPs applies to all business enterprises regardless of sector and size. Stakeholders have confirmed that there is no sector of business which does not pose any potential risks to human rights or the environment. Yet current laws and industry regulatory measures which only apply to certain sectors, products or commodities fail to prevent or address adverse impacts which take place outside of this sector. Examples include the EU conflict minerals regulation,[861] which only applies to companies sourcing tin, tantalum, tungsten and gold from conflict-affected and high risks areas, or the EU Timber Regulation[862] which applies to operators who place timber or timber products on the EU market.

Similar limitations apply to regulation which only applies to a specific issue, such as modern slavery or child labour. Stakeholders have indicated that these regulations result in processes which may overlook other human rights or environmental impacts.[863] For example, corporate due diligence processes which are limited to certain issues, such as child labour, have been found to be inadequate for the purposes of the OECD Guidelines' due diligence requirements by the Norwegian National Contact Point.[864] Scholars have also warned against the risk of disincentivising stronger forms of regulation.[865]

Evidence has shown that where companies fail to focus on the entire spectrum of human rights which they may potentially impact, they are significantly more likely to overlook human rights impacts in their own operations and in their supply chain.[866]

When presenting the "Protect, Respect and Remedy" Framework around which the UNGPs are based, John Ruggie, answering the call from certain stakeholders for focus on a limited list of human rights for which companies would have responsibility, stated that:[867]

> Business can affect virtually all internationally recognized rights. Therefore, any limited list will almost certainly miss one or more rights that may turn out to be significant in a particular instance, thereby providing misleading guidance.

The deliberate focus on the entire spectrum of human rights (often referred to as using the "human rights lens") also ensures that vulnerable groups are within the scope of the due diligence, including women, children, migrant workers and LGBTI individuals. For example, in the interviews conducted for this study stakeholders have raised the importance of including gender aspects in supply chain due diligence. A recent report by the UN Working Group on Business and Human Rights also highlighted the differentiated and disproportionate impact of business activities on woman and girls[868] and the

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[860] Elise Groulx Diggs, Milton C. Regan and Beatrice Parance, "Business and Human Rights as a Galaxy of Norms" (2019) 50:2 *Georgetown Journal of International Law* 309.
[861] Regulation (EU) 2017/821 of the European Parliament and of the Council of 17 May 2017 laying down supply chain due diligence obligations for Union importers of tin, tantalum and tungsten, their ores, and gold originating from conflict-affected and high-risk areas.
[862] Regulation (EU) No 995/2010 of the European Parliament and of the Council of 20 October 2010 laying down the obligations of operators who place timber and timber products on the market.
[863] See also Macchi and Bright, above n833.
[864] Norwegian National Contact Point for the OECD Guidelines for Multinational Enterprises, *Complaint from Lok Shakti Abhiyan, Korean Transnational Corporations Watch, Fair Green and Global Alliance and Forum for Environment and Development vs Posco (South Korea), ABP/APG (Netherlands) and NBIM (Norway)*, Final Statement, 27 May 2013.
[865] See also Ingrid Landau, "What are we missing by focusing on modern slavery?" (2016), available at: https://www.business-humanrights.org/en/what-are-we-missing-by-focusing-on-modern-slavery.
[866] McCorquodale, Smit, Neely and Brooks, above n823.
[867] UN Human Rights Council, "Protect, Respect and Remedy: A Framework for Business and Human Rights", A/HRC/8/5 (7 April 2008) at para 6.
[868] See UN Human Rights Council, "Gender dimensions of the Guiding Principles on Business and Human Rights: Report of the Working Group on the issue of human rights and transnational corporations and other business enterprises", A/HRC/41/43 (23 May 2019). See also on these issues Kelly Groen and Lis Cunha, "Due diligence laws must not leave women behind", *Business*

corresponding need for companies to apply a gender perspective to due diligence when appropriate and to make particular efforts to track the effectiveness of their responses to impacts on individuals from groups that may be at heightened risk of vulnerability, in line with the UNGPS and the OECD Due Diligence Guidance for Responsible Business Conduct.[869]

2.6 Lack of legal certainty about due diligence requirements for human rights and environmental impacts

Business stakeholders in particular report a high level of concern about the current lack of legal certainty about due diligence requirements for human rights and environmental impacts. This legal uncertainty arises because, even in the absence of a general legal duty for due diligence, companies are increasingly facing legal and other risks and costs[870] as a result of a failure to undertake due diligence.

Examples include:

- Companies are increasingly subject to high-profile lawsuits for alleged failure to prevent human rights or environmental harms.[871] These cases are often brought in tort law against parent companies for the harms caused by their subsidiaries, or even in the supply chain.[872]

- Various complaints have been filed in OECD NCPs on the basis of companies' failure to exercise due diligence for their human rights or environmental impacts, including by investee companies. Although the NCPs' statements are not legally binding, they are viewed as giving content to the due diligence which is expected from companies.[873]

- New laws or legal proposals are creating a patchwork of legislative requirements or expected legislative requirements (if proposed laws should be passed).[874] These laws are often applicable to multinational companies which operate across the relevant countries or sectors.

- Voluntary or non-binding standards, including the UNGPs and industry standards, are increasingly being used in civil law or tort claims to give content to the standard of care which was expected of the company in the relevant circumstances.[875] For instance, in its recent decision in *Lungowe v Vedanta*, the

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and Human Rights Resource Centre (25 June 2019), available at: https://www.business-humanrights.org/en/due-diligence-laws-must-not-leave-women-behind; Joanna Bourke Martignoni and Elizabeth Umlas, "Gender-Responsive Due Diligence for Business Actors: Human Rights-Based Approaches", *Geneva Academy, Academic Briefing No 12* (December 2018), available at: https://www.geneva-academy.ch/joomlatools-files/docman-files/Academy%20Briefing%2012-interactif-V3.pdf.

[869] UN Working Group Report ibid at paras 31 and 37.

[870] See for instance, Rachel Davis and Daniel Franks, "Costs of Company-Community Conflict in the Extractive Sector", *Corporate Social Responsibility Initiative Report N° 66* (2014), available at: https://www.hks.harvard.edu/sites/default/files/centers/mrcbg/programs/cri/files/Costs%20of%20Conflict_Davis%20%20Franks.pdf - a report that explores the costs of company-community conflict. The report explored the cost of failure to undertake appropriate due diligence resulting in conflict between companies and local communities in the extractive sector. The report revealed that "the most frequent costs were those arising from lost productivity due to temporary shut downs or delays [...] the greatest costs [...] were the opportunity costs in terms of lost value linked to future projects, expansion plans or sales that did not go ahead. The costs more often overlooked by companies were indirect costs resulting from staff being diverted to managing conflict - particularly senior management time - including in some cases that of the CEO".

[871] Marx, Bright and Wouters, above n826 at 18.

[872] For further examples see Section III Regulatory Review of this study.

[873] For instance, Clean Clothes Campaign Danmark and Aktive Forbrugere (Active Consumers) filed a complaint against the PWT Group to the Danish NCP in December 2014, alleging that PWT Group had failed to carry out due diligence in relation to its supplier, the textile manufacturer New Wave Style, to prevent the collapse of the Rana Plaza building in Bangladesh which housed the supplier. On this complaint, see: https://businessconduct.dk/file/631421/mki-final-statements.pdf.

[874] See for instance, BHRRC, "National movements for mandatory human rights due diligence in European countries", available at: https://www.business-humanrights.org/en/national-movements-for-mandatory-human-rights-due-diligence-in-european-countries.

[875] See for instance, in the Netherlands Court of Appeal of The Hague, *Eric Barizaa Dooh of Goi and others v Royal Dutch Shell Plc and Others*, 200.126.843 (case c) + 200.126.848 (case d), December 18, 2015; and in Canada *Araya v Nevsun Resources Ltd.*, 2016 BCSC 1856; *Choc v Hudbay Minerals Inc.*, 2013 ONSC 1414. On these issues, see for instance Claire Bright, "The

UK Supreme Court found that a parent company may owe a duty of care to the local communities affected by the operations of its foreign subsidiaries, based on the group-wide policies adopted by the parent company and its public commitments.[876] This is a particularly important case given the influential nature of UK case law in common law countries throughout the world, and the fact that it represents the "first decision by any superior court in the world directly on this issue".[877]

- Companies that are already taking extensive due diligence steps and dedicating significant resources to these matters report that they are sometimes being singled out and targeted for litigation.[878] Often, their voluntary commitments, global policies or efforts to undertake transparent reporting are being used to demonstrate an assumption of a duty of care or relationship of proximity with the claimants. Companies' legal advisers are faced with directly contradictory legal risks: the risks associated with a failure to implement global policies and processes to prevent and address human rights and environmental harms, as opposed to the risk of being sued on the basis of taking such proactive steps.[879]

The perceived targeting in litigation of those companies that are "leaders" is also a result of lack of legal certainty, insofar as claimants do not currently have a guaranteed legal basis to pursue those companies that have not taken these proactive steps.

A recent report from ClientEarth and Global Witness notes in this respect that:[880]

> [E]ffective due diligence is in the interest of companies themselves as environmental considerations can entail significant material risks. These can include operational blockages, as well as reputational, financial and legal risks. Legislation requiring companies to identify, prevent and mitigate environmental damage and human rights abuses can help them manage these risks and provide a level playing field for companies.

2.7 Lack of access to remedy for those affected by the adverse human rights or environmental impacts of EU companies

Currently, there is a well-documented lack of access to remedies for those affected by corporate human rights and environmental harms of EU companies.[881] This applies to persons affected within the EU, as well as outside of the EU.

Civil Liability of the Parent Company for the Acts or Omissions of Its Subsidiary: The Example of the *Shell* Cases in the UK and in the Netherlands" in Angelica Bonfanti (ed.), *Business and Human Rights in Europe: International Law Challenges* (Routledge, 2018) 212.

[876] *Lungowe v Vedanta Resources plc* [2019] UKSC 20, para 53: '*Even where group-wide policies do not of themselves give rise to such a duty of care to third parties, they may do so if the parent does not merely proclaim them, but takes active steps, by training, supervision and enforcement, to see that they are implemented by relevant subsidiaries. Similarly, it seems to me that the parent may incur the relevant responsibility to third parties if, in published materials, it holds itself out as exercising that degree of supervision and control of its subsidiaries, even if it does not in fact do so. In such circumstances its very omission may constitute the abdication of a responsibility which it has publicly undertaken.*'

[877] Robert McCorquodale, "Vedanta v. Lungowe Symposium: Duty of Care of Parent Companies" (18 April 2019), available at: http://opiniojuris.org/2019/04/18/symposium-duty-of-care-of-parent-companies/.

[878] This has been reported in our interviews and informational conversations with companies. See also Christopher Patz, "The Misuse of Abuse: Fears of Potentially Abusive Litigation are Overriding the Reality of Abusive Companies in Europe" (15 April 2018), available at: https://www.opendemocracy.net/en/can-europe-make-it/misuse-of-abuse-fears-of-potentially-abusive-litigation-are-over/.

[879] Peter Nestor and Jonathan Drimmer, "How Companies Should Respond to the Vedanta Ruling", *Business for Social Responsibility* (30 April 2019), available at: https://www.bsr.org/en/our-insights/blog-view/how-companies-should-respond-to-the-vedanta-ruling. See also Section II Market Practices in this study.

[880] ClientEarth and Global Witness, above n 814 at 3.

[881] Marx, Bright and Wouters, above n826; Jennifer Zerk, "Corporate liability for gross human rights abuses: Towards a fairer and more effective system of domestic law remedies. A report prepared for the Office of the UN High Commissioner for Human Rights", available at: https://www.ohchr.org/Documents/Issues/Business/DomesticLawRemedies/StudyDomesticeLawRemedies.pdf; Gwynne Skinner, Robert McCorquodale and Olivier De Schutter, "The Third Pillar: Access to Judicial Remedies for Human Rights Violations by Transnational Business", available at: http://corporatejustice.org/documents/publications/eccj/the_third_pillar_-access_to_judicial_remedies_for_human_rights_violation.-1-2.pdf; Amnesty International, "Injustice Incorporated: Corporate

Victims of corporate human rights abuses do not have any generally acknowledged or practically available access to remedies against multinational companies.[882] Harms often happen in (developing) host states in which victims frequently struggle to access legal remedies.[883] As a result, victims often attempt to bring their claims in the relevant multinational company's (developed) home state. However, even there they face many barriers to accessing legal remedies, both legal and practical. Examples of such barriers to access to remedies include:

- Difficulties and costs for claimants to secure legal representation[884]
- Resources and time required to prove claimants' onus and issues related to access to information[885]
- Restrictive time-limits on bringing claims[886]
- Immunities and non-justiciability doctrines[887]
- Jurisdictional challenges[888]
- Issues relating to the applicable law[889]
- The complexity of corporate structures and the attribution of legal responsibility among the members of a corporate group[890]
- Proving human rights violations[891]
- The reach and enforcement of remedies[892]

Many of these barriers stem from the fact that private international law envisage "corporate liability within the limits of compartmentalised, local law" but is "clearly out of touch with the global political economy".[893] The drivers of these barriers to access to remedy include:

- Traditional understandings of territorial jurisdiction have resulted in procedural hurdles for foreign defendants in host states to bring claims in companies' home states.[894] This corporate legal construct has been noted to be "extremely successful in facilitating business investment and the protection of shareholders' interests, but it has often led to unwanted outcomes for human rights and the environment".[895]

Abuse and the Human Right to Remedy" (2014), available at: https://www.amnesty.org/download/Documents/8000/pol300012014en.pdf.

[882] Marx, Bright and Wouters, ibid at 16.

[883] Ibid at 18.

[884] Amnesty International, above n881.

[885] Marx, Bright and Wouters, above n826 at 113.

[886] Skinner, McCorquodale and De Schutter, above n881 at 38.

[887] Ibid at 39.

[888] Marx, Bright and Wouters, above n826 at 114.

[889] Ibid at 116.

[890] Zerk, above n881 at 43.

[891] Skinner, McCorquodale and De Schutter, above n 881 at 43.

[892] Ibid at 62.

[893] Horatia Muir-Watt, "Private International Law Beyond the Schism" (2011) 2:3 *Transnational Legal Theory* 347 at 386.

[894] On these issues, see for instance Elena Blanco, "Jurisdiction, access to remedy in business and human rights cases and the corporate structure: A tale of two cases" (2019), available at: https://www.cambridge.org/core/blog/2019/05/07/jurisdiction-access-to-remedy-in-business-and-human-rights-cases-and-the-corporate-structure-a-tale-of-two-cases/.

[895] A report of the United Nations High Commissioner for Human Rights noted that: "The company law doctrine of 'separate corporate personality' is recognized in most, if not all, jurisdictions. Under this doctrine, each company, as a separately incorporated legal entity, is treated as having a separate existence from its owners and managers. Consequently, a company (a parent company) that owns shares in another company (a subsidiary) will not generally be held legally responsible for acts, omissions or liabilities of that subsidiary merely on the basis of the shareholding." UNHCHR, "Improving accountability and access to remedy for victims of business-related human rights abuse", A/HRC/32/19 (10 May 2016) at 9. In addition, Stephen Turner writes: "The second design feature is that corporate law around the globe facilitates limited liability for shareholders. This means that shareholders of 'limited liability' companies (which represent the vast majority) are not liable for all of the debts of a company; they are only liable up to the amount that they subscribed to through their share purchase. [...] As a result, where a company fails and enters into liquidation, the creditors of that business can naturally only seek to recover their debts from the shareholders to a limited extent. Similarly, where a company does not have sufficient funds to compensate those whose human rights it has negatively impacted or to remedy environmental degradation it has caused, the shareholders can enjoy protection from full liability." Stephen J. Turner, "Business practices, human rights and the environment" in James R. May and Erin Daly (eds.), *Human Rights and the Environment: Legality, Indivisibility, Dignity and Geography*, *Elgar Encyclopedia of Environmental Law* series (Edward Elgar Publishing, 2019) at 378. See also 376.

- The traditional concept of separate corporate personality allows companies to escape liability for the actions of others, including subsidiaries and suppliers, even where the relevant company had significant factual control over these entities.[896]

- The lack of specific European private international law rules adapted to the specificity of business-related human rights and environmental claims. A recent report commissioned by the European Parliament on the issue of access to justice for victims of corporate human rights abuses in third countries recommended, in this respect:

    - A revision of the Brussels I Recast Regulation in order to include in particular:

        - A provision extending the jurisdiction of the domicile of the defendant EU parent company to the claims over its foreign subsidiary or business partners when the claims are so closely connected that it is expedient to hear and determine them together.

        - A provision establishing a *forum necessitatis* on the basis of which the courts of an EU Member State may, on an exceptional basis, hear a case brought before them when the right to a fair trial or access to justice so requires, and the dispute has sufficient connection with the EU Member State of the court seized.

    - A revision of the Rome II Regulation in order to include in particular a choice-of law provision specific to business-related human rights claims against EU companies that would allow the claimant a choice between the law of the place where the damage occurred, the law of the place where the event giving rise to the damage occured and the law of the place where the defendant company is situated.

- The Victims' Rights Directive has fallen short of ensuring that victims of corporate crimes are afforded access to justice.

The third pillar of the UNGPs is about access to remedy, which is also a human right in itself (the right to remedy). Ensuring access to effective remedy for victims is a crucial part of both the State's duty to protect and the corporate responsibility to respect human rights. The OECD guidelines note, in relation to the due diligence processes of companies, that:

> Potential impacts are to be addressed through prevention or mitigation, while actual impacts are to be addressed through remediation.

In addition, Daniel Augenstein argues that "third-country victims seeking to vindicate their rights through transnational tort litigation in a European home state of MNCs come under that state's territorial authority and control within the meaning of Article 1 of the ECHR", and that, accordingly, domestic courts adjudicating their case "must comply with

[896] For instance, in the *Unilever* case, the English domiciled parent company and its Kenyan subsidiary were accused of complicity in human rights abuses by virtue of failing to protect its tea workers from the foreseeable risk of ethnic violence. The UK High Court and the Court of Appeal rejected the claims on the basis that the parent company did not owe a duty of care to the claimants. Similarly, in the *Shell* case, the UK Court of Appeal had rejected the claim against the parent company and its Nigerian subsidiary for health and environmental damage arising out of its activities in the Niger Delta on the basis that claimants could not demonstrate a properly arguable case that the parent company owed them a duty of care. However, the UK Supreme Court recently reaffirmed that a parent company may, in certain circumstances, owe a duty of care to the local communities re-affected by the activities of its subsidiaries. On this issue, see McCorquodale, above n877.

the state's international human rights obligations to ensure access to justice and effective civil remedies".[897]

The existing legal framework (both internationally and domestically) has failed to address the realities of transnational business in this respect. It is increasingly recognised that the limitations posed by traditional notions of territorial jurisdiction and separate corporate identity need to be updated to address the impacts of globalised supply chains and complex corporate groups. In addition, the remediation role performed by grievance mechanisms in connection to companies' supply chains remains extremely limited.[898]

3. Legal basis for and policy background of a possible future EU intervention

3.1 Legal basis for a possible future EU intervention

To address the problems as described in the previous section, any possible future EU intervention would be based on the following legal basis:

- The regulation of companies' due diligence requirements is a matter of company law which falls within the EU shared competences. In particular, Article 50(1) and (2)g of the Treaty on the Functioning of the European Union (TFEU) gives competence to the EU to act, by means of directives, to harmonise national company laws so as to attain freedom of establishment.[899] For example, the Non-Financial Reporting Directive (NFR Directive)[900] was adopted by the EU on this basis. In addition, Article 114 TFEU, in conjunction with Article 50, allows the EU to approximate legislation with the object of ensuring the proper functioning of the internal market.[901]

- The EU's regulatory competences in terms of promoting respect for human rights when adopting and implementing EU legislation, as well as with regard to its relationships with third countries, are grounded in the Treaty of the European Union (TEU). Article 2 of the TEU affirms that human rights are among the values upon which the EU has been founded, together with the respect for human dignity, freedom, democracy, equality and the rule of law.

- The Charter of Fundamental Rights of the European Union, which is legally binding, applies to the EU in all of its actions and to Member States whenever they implement EU law.[902] The Charter sets out a comprehensive framework for the duties to "respect, protect and promote", in line with the international human rights obligations[903] that are already binding on the EU Member States when implementing EU law.[904] Although it does not extend the EU competences, the

[897] Daniel Augenstein, "Torture as Tort? Transnational Tort Litigation for Corporate-Related Human Rights Violations and the Human Right to a Remedy" (2018) 18:3 *Human Rights Law Review* 593.
[898] See Market Practice section.
[899] ECCJ, "The EU Competence and Duty to Regulate Corporate Responsibility to Respect Human Rights through mandatory Human Rights Due Diligence", *ECCJ Briefing* (November 2017) at 2.
[900] Directive 2014/95/EU of the European Parliament and of the Council of 22 October 2014 amending Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups.
[901] Ibid at 2.
[902] European Commission SWD(2015), above n851 at 4.
[903] As discussed above in the context of EU Member States' obligations, the EU and its Member States have committed to a range of international human rights obligations through the various human rights treaties. These include the Universal Declaration of Human Rights, the International Covenant on Civil and Political Rights, the International Covenant on Economic, Social and Cultural Rights, the principles concerning fundamental rights in the eight ILO core conventions as set out in the Declaration on Fundamental Principles and Rights at Work, the International Convention on the Elimination of All Forms of Racial Discrimination, the Convention on the Elimination of All Forms of Discrimination against Women, the Convention against Torture and Other Cruel, Inhuman or Degrading Treatment or Punishment, the United Nations Convention on the Right of the Child, the International Convention on the Protection of the Rights of All Migrant Workers and Members of Their Families, the Convention on the Rights of Persons with Disabilities, the International Convention for the Protection of All Persons from Enforced Disappearance, the United Nations Declaration on the Rights of Indigenous People.
[904] Ibid at 4.

Charter requires the EU and the Member States to comply with human rights standards whenever EU law is implemented.[905]

- With regard to the Union's external action, Article 3.5 of the TEU provides that: "in its relations with the wider world, the Union shall uphold and promote its values and interests and contribute to the protection of its citizens. It shall contribute to peace, security, the sustainable development of the Earth, solidarity and mutual respect among peoples, free and fair trade, eradication of poverty and the protection of human rights, in particular the rights of the child, as well as to the strict observance and the development of international law, including respect for the principles of the United Nations Charter".

- Article 21.2 stipulates that "the Union shall define and purse common policies and actions, and shall work for a high degree of cooperation in all fields of international relations, in order to: [...] consolidate and support democracy, the rule of law, human rights and the principles of international law".

3.2 Policy background of a possible future EU intervention

In addition to the above legal obligations, the international and EU policy documents and strategies that are relevant for the intervention include the following (in chronological order). Some of these are discussed above in the context of EU Member States' international obligations and commitments, as well as in the TOR:

- The UN Convention to Combat Desertification in those countries experiencing serious drought and/or desertification, particularly in Africa[906]
- The Basel Convention on the Control of Transboundary Movements of Hazardous Wastes and Their Disposal[907]
- The Convention on International Trade in Endangered Species of Wild Fauna and Flora[908]
- The UNECE Aarhus Convention on Access to Information, Public Participation in Decision-making and Access to Justice in Environmental Matters[909]
- The Cartagena Protocol on Biosafety[910]
- Directive 2004/35/CE of the European Parliament and of the Council of 21 April 2004 on environmental liability with regard to the prevention and remedying of environmental damage
- The UN Guiding Principles on Business and Human Rights[911]
- The UN Human Rights Council Resolution on the Elaboration of an international legally binding instrument on transnational corporations and other business enterprises with respect to human rights, establishing an open-ended intergovernmental working group on transnational corporations and other business[912]
- The Paris Agreement on climate change[913]
- The UN 2030 Agenda for Sustainable Development[914]
- The ILO Tripartite declaration of principles concerning multinational enterprises and social policy (MNE Declaration)[915]

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[905] Ibid at 4.
[906] 1994, available at: https://www.unccd.int/sites/default/files/relevant-links/2017-01/UNCCD_Convention_ENG_0.pdf.
[907] 1989, available at: http://www.basel.int/theconvention/overview/tabid/1271/default.aspx.
[908] 1973, available at: https://www.cites.org/eng/disc/what.php.
[909] 1998, available at: https://www.unece.org/env/pp/treatytext.html.
[910] 2000, available at: http://bch.cbd.int/protocol/text/.
[911] Discussed at length in previous sections.
[912] Resolution A/HRC/RES/26/9 (14 July 2014), available at: http://ap.ohchr.org/documents/dpage_e.aspx?si=A/HRC/RES/26/9.
[913] Available at: https://unfccc.int/process-and-meetings/the-paris-agreement/the-paris-agreement.
[914] Available at: http://ec.europa.eu/environment/sustainable-development/SDGs/index_en.htm.
[915] 2017, available at: https://www.ilo.org/empent/areas/mne-declaration/lang--en/index.htm.

- The 2016 ILO Resolution concerning decent work in global supply chains[916]
- The ILO Centenary Declaration for the Future of Work[917]
- The 2017 G20 Leaders' declaration on Sustainable Global Supply Chains[918]
- The 2017 G20 declaration of Employment and Labour Ministers[919]
- The 2019 G7 Communiqué of Employment and Labour Ministers[920]
- The European Commission Communication of 22 November 2016 "Next steps for a sustainable European future"[921]
- The European Parliament Resolution of 27 April 2017 on the EU flagship initiative on the garment sector[922]
- The Council conclusions on the EU and Responsible Global Value Chains[923]
- The European Commission Staff Working Document on Sustainable garment value chains[924]
- The Council of the European Union Conclusions on business and human rights, 20 June 2016
- The Victims' Rights Directive[925]
- The Council of Europe Recommendation to Member States on the implementation of the UNGPs by Member States[926]
- The Stockholm Convention on persistent organic pollutions (POPs), revised in 2017[927]
- The High-Level Expert Group on Sustainable Finance (HLEG) Final Report, 31 January 2018[928]
- The European Commission Action Plan on Financing Sustainable Growth (Action Plan on Sustainable Finance) of 2018[929]
- The European Commission Report on Critical Raw Materials and the Circular Economy
- The European Parliament report on sustainable finance of 4 May 2018[930]
- The European Parliament Report on the proposal for a Regulation of the European Parliament and of the Council on the alignment of reporting obligations in the field of environment policy of 15 October 2018[931]
- The European Commission Report on the implementation of the Circular Economy Action Plan[932]
- The European Commission strategic long-term vision for a prosperous, modern, competitive and climate neutral economy[933]

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[916] Available at: https://www.ilo.org/ilc/ILCSessions/previous-sessions/105/texts-adopted/WCMS_497555/lang--en/index.htm.
[917] 2019, available at: https://www.ilo.org/ilc/ILCSessions/108/reports/texts-adopted/WCMS_711674/lang--en/index.htm.
[918] Available at: http://www.g20.utoronto.ca/2017/2017-G20-leaders-declaration.pdf.
[919] Available at: http://www.g20.utoronto.ca/2017/170519-labour.html.
[920] Available at: https://travail-emploi.gouv.fr/IMG/pdf/g7_social_communique_and_outcomes_final.pdf.
[921] Available at: https://www.eesc.europa.eu/en/our-work/opinions-information-reports/opinions/next-steps-sustainable-european-future.
[922] Available at: http://www.europarl.europa.eu/doceo/document/TA-8-2017-0196_EN.html?redirect.
[923] Available at: http://data.consilium.europa.eu/doc/document/ST-8833-2016-INIT/en/pdf.
[924] European Commission, "Commission Staff Working Document on sustainable garment value chains through EU development action", SWD(2017) 147 final.
[925] Directive 2012/29/EU of the European Parliament and of the Council of 25 October 2012 establishing minimum standards on the rights, support and protection of victims of crime, and replacing Council Framework Decision 2001/220/JHA.
[926] Available at: https://edoc.coe.int/en/fundamental-freedoms/7302-human-rights-and-business-recommendation-cmrec20163-of-the-committee-of-ministers-to-member-states.html.
[927] Available at: http://www.pops.int/TheConvention/Overview/TextoftheConvention/tabid/2232/Default.aspx.
[928]Available at: https://ec.europa.eu/info/publications/180131-sustainable-finance-report_en.
[929] Communication from the Commission to the European Parliament, the European Council, the Council, the European Central Bank, the European Economic and Social Committee and the Committee of the Regions "Action Plan: Financing Sustainable Growth", COM/2018/097 final, available at: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52018DC0097.
[930] Available at: http://www.europarl.europa.eu/doceo/document/A-8-2018-0164_EN.html.
[931] European Parliament Report on the proposal for a Regulation of the European Parliament and of the Council on the alignment of reporting obligations in the field of environment policy and thereby amending Directives 86/278/EEC, 2002/49/EC, 2004/35/EC, 2007/2/EC, 2009/147/EC and 2010/63/EU, Regulations (EC) No 166/2006 and (EU) No 995/2010, and Council Regulations (EC) No 338/97 and (EC) No 2173/2005(COM(2018)0381 – C8-0244/2018 – 2018/0205(COD)), 15 October 2018, available at: http://www.europarl.europa.eu/doceo/document/A-8-2018-0324_EN.html.
[932] Report from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions on the implementation of the Circular Economy Action Plan, COM(2019) 190 final, http://ec.europa.eu/environment/circular-economy/pdf/report_implementation_circular_economy_action_plan.pdf.
[933] Communication from the Commission to the European Parliament, the European Council, the Council, the European Economic and Social Committee, the Committee of the Regions and the European Investment Bank "A Clean Planet for all: A

- The EU Communication (2019) on Stepping up EU Action to Protect and Restore the World's Forests.[934]

3.3 Calls for mandatory due diligence at EU level based on legal and policy background

It is also noted that recent observations about, or calls for, mandatory due diligence at EU level have referred to the existing policy framework relating to its EU's international obligations, commitments and responsibilities. Some of these include:

- In 2016, Members of Parliaments of eight Member States, prompted by Member of the French Parliament Danielle Auroi, launched a "green card" initiative calling for "duty of care legislation protecting individuals and communities whose human rights and local environment are affected by the activity of EU-based companies" at the EU level.[935]

- In its Legal Opinion on improving access to remedy in the area of business and human rights at the EU level, the EU Agency for Fundamental Rights also called for "stronger legislative incentives" modelled on the French Law on the Duty of Vigilance.[936]

- In March 2019, the Responsible Business Conduct Working Group (RBC Group) of the European Parliament presented its Shadow EU Action Plan on the implementation of the UNGPs.[937] The Shadow EU Action Plan recommended, as a first step, for the Commission and the EEAS to come forward with an EU Action Plan on the Implementation of the UNGPs.[938] As part of its recommendations on the implementation of Pillar I of the UNGPs, the Shadow EU Action Plan mentioned the adoption of mandatory due diligence for EU businesses and businesses operating within the EU which would require them to carry out human rights due diligence regarding their operations, investments, business relationships and supply chains. The Shadow Action Plan specifies that "due diligence procedures need to take into account the specific risks and differentiated impacts of business-related activities on women, youth and other marginalised groups and communities".[939] It also provided, as part of its recommendation on the implementation of Pillar III of the UNGPs, for the adoption of legislation "establishing liability of companies for environmental or human rights harm, based on the principle of reasonable care, including for damage caused by companies under their control".[940] The Shadow EU Action Plan stated that:[941]

  > It is urgent time for the EU, which is directly bound by its treaties to promote and protect human rights globally, to take action. The EU is the

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European strategic long-term vision for a prosperous, modern, competitive and climate neutral economy", COM(2018) 773 final, 28 November 2018, available at: https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52018DC0773&from=en.

[934] Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions: Stepping up EU Action to Protect and Restore the World's Forests, COM(2019) 352 final, 23 July 2019, available at: https://ec.europa.eu/info/sites/info/files/communication-eu-action-protect-restore-forests_en.pdf.

[935] ECCJ, "Members of 8 European Parliaments support duty of care legislation for EU corporations" (18 May 2016), available at: http://corporatejustice.org/news/132-members-of-8-european-parliaments-support-duty-of-care-legislation-for-eu-corporations.

[936] FRA, "Improving Access to Remedy in the Area of Business and Human Rights at the EU Level" (10 April 2017), available at: https://fra.europa.eu/sites/default/files/fra_uploads/fra-2017-opinion-01-2017-business-human-rights_en.pdf.

[937] Responsible Business Conduct Working Group, "Shadow EU Action Plan on the Implementation of the UN Guiding Principles on Business and Human Rights within the EU" (March 2019), available at: https://responsiblebusinessconduct.eu/wp/wp-content/uploads/2019/03/SHADOW-EU-Action-Plan-on-Business-and-Human-Rights.pdf.

[938] Ibid at 2.

[939] Ibid at 6.

[940] Ibid at 10.

[941] Ibid at 1.

> world's largest economy, a trading hub with significant economic and political power to influence the regulation of economic operations worldwide. The EU and its member states are also increasingly subsidizing European companies operating in developing and neighbouring countries. It therefore carries a particular responsibility to prove leadership in the promotion and protection of human rights against business-related human rights abuses.[942]

In addition, recent trends have witnessed support for mandatory human rights due diligence regulation at both national and EU level from certain large multinational corporations. For instance, a number of companies joined the coalition campaign which resulted in the Finnish Government committing to mandatory human rights legislation in Finland,[943] and the Swiss Association Groupement des Entreprises Multinationales (representing over 90 companies) expressed its support for the Swiss legislative (counter) proposal.[944] In addition, several major chocolate companies have publicly called for an EU level regulation on mandatory human rights due diligence.[945]

In relation to climate change, scholars have argued that:[946]

> The EU continues to play the role of a leading global actor in the adoption of innovative climate-related policy frameworks, some of which specifically concern the link between business activities and climate change. In this respect, significant developments in the EU regulatory framework have already taken place, and more are to be expected in the future.

4. Intervention logic of a possible future EU intervention

Based on the Problem Analysis, the description of the legal basis and the policy background of a possible EU intervention (as presented above), the following general and specific objectives for a possible future EU intervention is suggested:

Proposed general objectives of a possible future EU intervention:

- To promote adherence to international and EU human rights and environmental obligations and commitments, including relating to climate change.
- To mainstream sustainability as an essential guiding principle for all EU policies, including with respect to corporate governance.[947]
- To deliver on the Sustainable Development Goals (especially SDG 12) and the Paris Agreement.
- To foster a more long-term orientation in business.

Proposed specific objectives of a possible future EU intervention:

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[942] Ibid at 1.
[943] Finnwatch, "Finnish Government commits to HRDD legislation" (3 June 2019), available at: http://corporatejustice.org/news/15476-finnish-government-commits-to-hrdd-legislation.
[944] Maude Bonvin, "Entreprises mises devant leurs responsabilités" (15 June 2018), available at: https://www.gemonline.ch/uploads/_Files/documents_publics/Revue_de_presse/2018/2018.06.15_Agefi_Entreprises%20mises%20devant%20leurs%20responsabilites.pdf.
[945] Fern, "Chocolate companies and MEPs call for EU Due Diligence Regulation" (10 April 2019), available at: https://www.fern.org/news-resources/chocolate-companies-and-meps-call-for-eu-due-diligence-regulation-954/.
[946] Chiara Macchi, "Climate Change, Business and Human Rights in the European Context: An Emerging Area of Legal Risk", draft paper presented at the conference "Justice for Transnational Human Rights Violations At the Crossroads of Litigation, Policy and Scholarship", Bonavero Institute of Human Rights (Oxford) on 19-20 June 2019 (on file with the author) at 2. See also Charles F. Parker, Christer Karlsson and Mattias Hjerpe, "Assessing the European Union's global climate change leadership: from Copenhagen to the Paris Agreement" (2017) 39:2 Journal of European Integration 239.
[947] Terms of Reference (TOR) at 3; Commission Communication of November 2016 "Next steps for a sustainable European future".

- To help prevent adverse human rights and environmental impacts in the context of business activities.
- To clarify companies' due diligence obligations for human rights and the environment, including climate change.
- To foster more sustainable corporate governance.
- To ensure that companies implement processes to carry out due diligence to prevent human rights or environmental abuses or damage.
- To avoid fragmentation of due diligence requirements across sectors of industry, Member States and area of application.
- To establish sanctions or liability for abuses that a company is involved in or could have prevented.
- To provide access to remedy for those affected by the adverse human rights or environmental impacts of EU companies.

These proposed general and specific objectives of a possible future EU intervention also take into account the description of the background of the study as described in the TOR and the findings of the study.

Based on the problem analysis and the definition of objectives it is then possible to elaborate the intervention logic of a possible future EU initiative. It considers the underlying "theory" of the intervention (how it would be expected to work), as derived from the analysis of the study. The following figure presents the proposed intervention logic and shows how the identified problems and needs relate to the proposed general and specific objectives, as well as to the expected inputs/activities, the intended outputs and results, as well as the wider impacts.

Note that the intervention logic focuses on a comprehensive EU initiative, in line with Option 4 presented below. If another option would be preferred, the intervention logic would need to be adapted accordingly. For example, if no remedy was provided for those affected, potential impacts in this respect could not be expected and would have to be removed from the intervention logic.

Intervention logic of a possible EU intervention

Needs/Problems

- Adverse human rights and environmental impacts in global supply and value chains, aggravated by their increasingly complex, dynamic and non-transparent character
- Global climate change crisis which requires coordinated approach from business and governments
- Predominantly short-term focus of companies which affects their ability to integrate sustainability into their strategies and risk management and develop sustainable business models
- Failure of corporate risk assessment processes to extend beyond the risks of the company to those who are actually or potentially affected by its supply and value chain
- Lack of implementation of due diligence by companies, despite some transparency and reporting requirements
- Lack of reliable information to enhance the ability of consumers and investors to make sustainable choices
- Regulatory gap between current legal framework and Member States' international and EU human rights and environmental obligations
- Increasing fragmentation of due diligence requirements across sectors, size of companies, countries and area of application
- Lack of legal certainty for companies about due diligence requirements for human rights and environmental impacts, including on climate change
- Lack of access to remedy for those affected by the adverse human rights or environmental impacts of EU companies

Objectives

Global objectives

- To promote adherence to international and EU human rights and environmental obligations and commitments, including relating to climate change
- To mainstream sustainability as an essential guiding principle for all EU policies, including with respect to corporate governance
- To deliver on the Sustainable Development Goals (esp. SDG 12) and Paris Agreement
- To foster a more long-term orientation in business

Specific objectives

- To help prevent adverse human rights and environmental impacts in the context of business activities
- To clarify companies' due diligence obligations for human rights and the environment, including climate change
- To foster more sustainable corporate governance
- To ensure that companies implement processes to carry out due diligence to prevent human rights or environmental abuses or damage
- To avoid fragmentation of due diligence requirements across sectors of industry, Member States and area of application
- To establish sanctions or liability for abuses that a company is involved in or could have prevented
- To provide access to remedy for those affected by the adverse human rights or environmental impacts of EU companies

Inputs/activities

- Implementation of changes to the regulatory framework
- Implementation of due diligence obligations by companies (including e.g. assessing risks, changes to internal processes, training, audits, engagement with suppliers/local stakeholders, reorganisation of supply chains, monitoring, communicating/reporting, etc.)
- Enforcement of due diligence obligations of companies (including by provision of remedies for those affected)

Outputs/results

- Regulatory framework better aligned with Member States' international and EU human rights and environmental obligations, including relating to climate change
- Uniform EU-wide standard for due diligence provided
- Companies' due diligence obligations for human rights and the environment are clarified, including relating to climate change
- Fragmentation of supply chain due diligence requirements across sectors of industry, Member States and area of application is avoided
- Corporate risk assessment processes include risks for those who are actually or potentially affected by their supply and value chains
- Improved corporate accountability and transparency with respect to risks of adverse human rights and environmental impacts in supply and value chains
- Liability established for human rights or environmental abuses that a company is involved in and could have prevented
- Remedies for those affected by the adverse human rights or environmental impacts of EU companies

Impacts

- Sustainability is mainstreamed as essential guiding principle for EU policies with respect to corporate governance
- More innovation resulting from transition to a greener economy
- Coordination between business and governments to address global climate change crisis is improved
- Level playing field for EU companies with respect to due diligence obligations
- Long-term value creation and sustainability better integrated into corporate governance arrangements
- Corporate culture for responsible management of supply and value chains established
- Improved implementation of due diligence by companies to reduce risks of human rights or environmental abuses/damage
- Reduced adverse human rights and environmental impacts (e.g. less CO_2 emissions, deforestation, biodiversity loss etc.) throughout corporate global supply and value chains
- Adherence to international and EU human rights and environmental obligations and commitments is promoted
- Human rights or environmental abuses in global supply and value chains are sanctioned, and remediation to those affected for harms suffered
- Benefits of globalisation are more fairly shared in line with the EU principles of solidarity and sustainability

5. Regulatory options

The regulatory options considered during this study, which will also form the basis of the assessment of the regulatory options in the following section, are as follows:

Option 1: No policy change (baseline scenario)
Option 2: New voluntary guidelines / guidance
Option 3: New regulation requiring due diligence reporting
Option 4: New regulation requiring mandatory due diligence as a legal duty of care:
- Sub-option 4.1: New regulation applying to a narrow category of business (limited by sector);
- Sub-option 4.2: New regulation applying horizontally across sectors:
  - Sub-option 4.2(a): applying only to a defined set of large companies;
  - Sub-option 4.2(b): applying to all business, including SMEs.
  - Sub-option 4.2(c): 4.2 (c) general duty applying to all business plus specific additional obligations only applying to large companies
- Sub-option 4.3: Sub-options 1 and 2 accompanied by a statutory oversight and / or enforcement mechanism:
  - Sub-option 4.3(a): mechanisms for judicial or non-judicial remedies;
  - Sub-option 4.3(b): state-based oversight body and sanction for non-compliance.

5.1 No policy change (baseline scenario)

This option would entail no changes at all in regulation at EU level for companies on undertaking due diligence through the supply chain. The existing regulatory position is described in the Regulatory Review.

There is currently no general legal duty at EU level to require companies across all sectors to exercise mandatory supply chain due diligence for their human rights and environmental impacts.

The status quo is currently a mix of different legal obligations and standards which are expected of companies. Some of these are legal, as set out in terms of regulation or case law, and some are industry standards or "soft law". Some of these due diligence standards only apply within specific industries or sectors.

The scope and content of existing requirements for due diligence varies from jurisdiction to jurisdiction. Some apply only with respect to certain human rights issues such as modern slavery, forced labour, human trafficking or child labour, whilst others apply across human rights and environmental issues. Some focus on different sectors or commodities, such as timber or conflict minerals, whilst others are cross-sectoral.

These laws also contain different due diligence requirements. Some take the form of legislation which requires reporting on due diligence (see Option 3 below), whereas the French Duty of Vigilance Law and various legislative proposals that are currently pending require companies to undertake mandatory due diligence in their operations and throughout their supply chains (see Option 4 below). These laws vary with respect to the scope of liability within the corporate group and supply chain, and in terms of providing for right to civil remedy and enforcement mechanisms. Existing EU and domestic regulation have also been introduced for the protection of the environment, some of which are set out in Part IV Annexure C 3: Table of selected EU laws and voluntary standards for environmental protection.

Existing laws also vary in terms of their scope of application to different types of companies. Some apply only to companies of a certain (large) size, based on turnover or employee numbers, whilst others apply to companies regardless of size. Some requirements are limited to companies domiciled in the regulating State whilst others extend to companies which operate or carry out business in that State.

In a report for the Office of the UN High Commissioner for Human Rights, Jennifer Zerk describes the current legal landscape as follows:[948]

> [T]he present system of domestic law remedies is patchy, unpredictable, often ineffective and fragile. It is failing victims who are unable in many cases to access effective remedies for the abuses they have suffered. It is failing some States because of the implications of current patterns of use of remedial mechanisms for capacity-building and legal development. And it is failing many companies, which are obliged to operate in an environment of great legal uncertainty and where participants are not competing on anything approaching a level playing field with respect to legal standards and levels of legal and commercial risk.

The current regulatory framework is discussed in full in the Regulatory Review section, but the status quo may be summarised as follows:

- The origin of the concept of due diligence for human rights (and environmental) impacts is the UN Guiding Principles on Business and Human Rights ("the UNGPs"). The UNGPs first introduced the concept of human rights due diligence ("HRDD") to as a way in which to "identify, prevent, mitigate and account for"[949] actual or potential adverse human rights impacts a company may be involved in through its own activities or business relationships.

- Since the UNGPs, other international frameworks have incorporated expectations on HRDD, including the OECD Guidelines for Multinational Enterprises,[950] the ILO Tripartite declaration of principles concerning multinational enterprises and social policy (MNE Declaration, the OECD Guidance on Responsible Business Conduct,[951] which applies to the supply chain, and OECD sectoral guidance on due diligence for certain sectors,[952] such as those related to conflict minerals,[953] the agricultural sector,[954] the garment and footwear sector,[955] and institutional investors.[956] The OECD Guidelines also require OECD Member States to establish National Contact Points ("NCPs"), to which complaints may be submitted for companies' failure to meet the OECD standards, including their due diligence requirements.

- The EU has instituted a number of initiatives imposing certain HRDD obligations, such as, the EU Non-Financial Reporting Directive,[957] the EU Timber Regulation,[958] and the EU Conflict Minerals Regulation.[959]

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[948] Zerk, above n881 at 7.
[949] Terms of Reference (TOR) at 3; Commission Communication of November 2016 "Next steps for a sustainable European future".
[949] UNGP 15.
[950] OECD, above n848.
[951] The HRDD was incorporated into the OECD Guidelines as part of the 2011 revision.
[952] OECD, above n848,, "Commentary on General Policies" at 21 para 14.
[953] OECD, "Due Diligence Guidance for Responsible Supply Chain of Minerals from Conflict-Affected Areas" (2016).
[954] OECD-FAO, "Guidance for Responsible Agricultural Supply Chains" (2016).
[955] OECD, "Due Diligence Guidance for Responsible Supply Chains in the Garment and Footwear Sector" (2017).
[956] OECD, "Responsible Business Conduct for Institutional Investors: Key Considerations for due diligence under the OECD Guidelines for MNEs" (2016).
[957] EU Non-Financial Reporting Directive, above n900.
[958] Regulation (EU) No 995/2010, above n862.
[959] Regulation (EU) 2017/821, above n861.

The 2017 French Duty of Vigilance law[960] is the only legislative example to date which imposes a general mandatory due diligence requirement for human rights and environmental impacts. As this law is new, there are not yet any court decisions which clarify how this law will be applied. However, during the course of this study, the first litigations in terms of this law have been instituted.[961] A Dutch Child Labour Due Diligence Law was adopted during the course of this study. The Italian Legislative Decree 231/2001,[962] provide for a defence from corporate criminal liability against certain offences if the company can demonstrate that it adopted "models of organisation, management and control" in order to identify, prevent and mitigate the risk of commission of certain human rights and environmental violations.[963]

In Switzerland there are pending proposals for mandatory human rights due diligence laws,[964] and discussions relating to such laws are taking place in Finland, Germany[965] and Norway.[966] Campaigns for mandatory human rights due diligence laws have also been launched in Austria, Belgium, Denmark, Finland, Germany, Luxembourg, the Netherlands, Norway, Sweden and the UK.[967]

Some legislative measures require reporting requirements with respect to certain human rights impacts only, particularly modern slavery and forced labour. Examples include the UK Modern Slavery Act and the Australia Modern Slavery Act, which both succeeded the 2010 California Transparency in Supply Chains Act.[968] Proposals for similar modern slavery acts have been made in Hong Kong and New Zealand. In addition the Dutch Child Labour Due Diligence Law that was passed in May 2019 focuses on issues of child labour.[969]

Anti-corruption laws often require due diligence through the supply chain, and failure to exercise this could be a criminal offence, also exposing individual directors to criminal liability. For example, the US Foreign Corrupt Practices Act[970] and the UK Bribery Act 2010 provide for due diligence as a defence to liability.

Apart from the French Duty of Vigilance Law, which is too new to have generated case law to date (the first legal actions having just been instituted on that basis), there is currently no direct cause of action to sue a company for human rights violations. Claimants have pursued alternative avenues to bring such claims, including in terms of tort law (often against parent companies for harms which took place through the

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[960] Law No. 2017-399 of March 27, 2017 on the "Duty of Vigilance of Parent Companies and Ordering Companies".
[961] See Regulatory Review, section 3.2.6
[962] Decreto Legislativo 8 giugno 2001, n. 231, *Disciplina della responsabilità amministrativa delle persone giuridiche, della società e delle associazioni anche prive di personalità giuridica*, a norma dell'articolo 11 della legge 29 settembre 2000, n. 300, pubblicato nella Gazzetta Ufficiale n. 140 del 19 giugno 2001. See Regulatory Review and Italy Country Report.
[963] FIDH, HRIC and ECCJ, "Italian Legislative Decree No. 231/2001: A model for Mandatory Human Rights Due Diligence Legislations?", November 2019, available at: https://e6e968f2-1ede-4808-acd7-cc626067cbc4.filesusr.com/ugd/6c779a_d800c52c15444d74a4ee398a3472f64c.pdf, at 10.
[964] Swiss Coalition for Corporate Justice ("SCCJ"), "The Initiative Text with Explanations", available at: https://corporatejustice.ch/wp-content/uploads//2018/06/KVI_Factsheet_5_E.pdf; SCCJ, "How does the parliamentary counter-proposal differ from the popular initiative (RBI)?", May 2018, available at: https://corporatejustice.ch/wp-content/uploads/2018/07/Comparision_RBI_counter-proposal_EN-1.pdf.
[965] Business and Human Rights Resource Centre ("BHRRC"), "German Development Ministry drafts law on mandatory human rights due diligence for German companies", available at: https://www.business-humanrights.org/en/german-development-ministry-drafts-law-on-mandatory-human-rights-due-diligence-for-german-companies. It is noted that the German Federal Government recently issued a statement stressing that the document merely constitutes "internal considerations" within the German Federal Ministry for Industrial Cooperation and Development ("BMZ"), https://www.bundestag.de/presse/hib/670510-670510. See also Manfred Shäfers "Regiering droht mit einem Lieferkettengesetz", *Frankfurter Allgemeine*, 11 December 2019; Caspar Dohmen, "Minister arbeiten an Lieferkettengesetz", *Süddeutsche Zeitung*, 11 December 2019.
[966] Report from the Ethics Information Committee, appointed by the Norwegian government on June 1, 2018. Report delivered on November 28, 2019. Draft translation from Norwegian of sections of Part I. Available at: https://www.business-humanrights.org/sites/default/files/documents/Norway%20Draft%20Transparency%20Act%20-%20draft%20translation_0.pdf
[967] BHRRC, "National Movements for Mandatory Human Rights Due Diligence in European Countries", available at: https://www.business-humanrights.org/en/national-movements-for-mandatory-human-rights-due-diligence-in-european-countries.
[968] California Transparency in Supply Chains Act of 2010.
[969] The Netherlands Child Labour Due Diligence Act 2019.
[970] US Foreign Corrupt Practices Act 15 USCs78dd-1 (1977).

activities of a foreign subsidiary), and consumer protection laws. Some legal claims are being instituted based on individual defendant companies' role in climate change.[971] This is an area which is new and developing.

In the absence of EU regulation on due diligence, it is expected that:

- Domestic legal frameworks will increasingly introduce mandatory due diligence requirements for human rights and environmental due diligence. They are likely to follow the concept of due diligence as described in the UNGPs, but may differ in terms of application of scope, implementation, and enforcement.

- This will take place both within EU Member States as well as elsewhere. For example, in France the Duty of Vigilance Law is already in force. Similar proposals have been made in Germany, Finland, Belgium, as well as the UK and Switzerland. (In the Netherlands, the Dutch Child Labour Due Diligence Law was passed in May 2019).[972] Acts which require reporting on due diligence for modern slavery have taken effect in the UK and Australia, and have been proposed in Hong Kong and New Zealand.

- Some EU Member States are unlikely to introduce due diligence measures, which will lead to a patchwork of due diligence expectations across the EU.

- Victims will still continue to face a lack of access to remedies, apart from in those countries where mandatory due diligence measures is introduced and rights to civil remedies are thereby created.

- At EU level, existing and anticipated due diligence requirements applicable only to certain sectors or issues, such as the EU Timber Regulation, the EU Conflict Minerals Regulation, the EU General Data Protection Regulation, and the proposed EU Regulation on disclosures relating to sustainable investments and sustainability risks.[973]

This will continue to lead to a situation where companies are subject to such requirements and others are excluded. Increasingly, the same company may be covered by more than one of these requirements at EU and/or Member State level.

5.2 New voluntary guidelines/guidance (Option 2)

This option would entail new voluntary guidelines at EU level for companies on undertaking due diligence through the supply chain. Voluntary guidelines are by their nature not usually legally enforceable. However, they may influence the standard required under specific circumstances or in specific industries, which in turn may be taken into account in civil claims, such as in tort law or contracts.

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[971] BHRRC, above n804 at 1.
[972] The Netherlands Child Labour Due Diligence Act 2019.
[973] European Parliament legislative resolution of 18 April 2019 on the proposal for a regulation of the European Parliament and of the Council on disclosures relating to sustainable investments and sustainability risks and amending Directive (EU) 2016/2341, Article 3gamma, entitled "Transparency of adverse sustainability impacts at entity level", provides in particular that:

1. Financial market participants shall publish and maintain on their websites either of the following: a) where they consider principal adverse impacts of investment decisions on sustainability factors, a statement on due diligence policies with respect to these principal adverse impacts, taking due account of their size, nature and scale of their activities and the types of their financial products; b) where they do not consider adverse impacts of investment decisions on sustainability factors, clear reasons for not doing so, and, where relevant, including information as to whether and when they intend to consider such adverse impacts. 2. Information provided in accordance with point (a) of the paragraph 1 shall include at least the following: a) information on policies on the identification and prioritisation of principal adverse sustainability impacts and indicators; b) a description of the principal adverse sustainability impacts and of the actions taken and, where relevant, planned; c) brief summaries of engagement policies in accordance with Article 3g of Directive 2007/36/EC, where applicable; d) reference to the adherence to responsible business conduct codes and internationally recognised standards for due diligence and reporting and, where relevant, the degree of alignment with the long-term global warming targets of the Paris Climate Agreement.

Examples of influential guidelines which already exist in this context include the UN Guiding Principles on Business and Human Rights, and the OECD Guidelines for Multinational Enterprises. These guidelines have been followed by various others, including a wealth of industry guidance.

As highlighted above, various voluntary guidelines already exist relating to due diligence for human rights and environmental impacts of business. These guidelines, in particular the UNGPs, the OECD Guidelines and certain industry standards, have been shown in our surveys and interviews to be influential and informs the way in which companies think about their due diligence. These guidelines have been followed by various others, including a wealth of industry guidance.

It has been observed both by stakeholders in our study as well as external commentators, that the limitations of voluntary guidelines lie in the fact that they are soft law instruments, and as such do not give rise to legally binding obligations.[974] As a result, despite the influence of the UNGPs, the actual implementation of due diligence obligations for human rights and environmental impacts by businesses has been very poor in practice.

For example, in 2018, the Corporate Human Rights Benchmark assessment of 101 of the world largest publicly traded companies across three industries (agricultural products, apparel and extractives) found that a majority of companies scored poorly on the Benchmark, with 40% of companies scoring no points at all across the due diligence section of the assessment.[975] According to the report, "this should provide food for thought for governments considering the role of legislation in business and human rights and should also serve as a wake-up call for businesses and investors everywhere".[976]

Another example can be provided by the cocoa sector for which a report from Mighty Earth revealed that a year after the pledge of the world's largest chocolate and cocoa companies, the sourcing of cocoa linked to deforestation continued, and that "big companies as well as the governments of Côte d'Ivoire and Ghana hold responsibility for this continued – but avoidable – destruction":[977]

> While some companies and local authorities have taken actions to limit deforestation, and some areas saw improvements, we nonetheless documented that farmers who engaged in deforestation for cocoa were still able to openly sell their cocoa without repercussions. Farmers we caught openly clearing forest for cocoa told us that they did not face sanctions, discontinued supply chains, or even warnings from the buyers in Cargill's and other companies' supply chains.

Another recent report noted that:[978]

> There have been many voluntary initiatives to tackle these problems. The use of certification schemes for cocoa is more common than for most agricultural commodities, a new International Organisation for Standardisation (ISO) standard for sustainable cocoa has been published, and many companies have their own programmes. Organisations and initiatives have been set up to tackle

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[974] See Section 2 Market Practices.
[975] CHRB, "2018 Key Finding - Apparel, Agricultural Products and Extractives Companies", available at: https://www.corporatebenchmark.org/sites/default/files/documents/CHRBKeyFindings2018.pdf at 5 and 13.
[976] Ibid at 5.
[977] Etelle Higonnet, Glenn Hurowitz, Abdul Tejan Cole, Alex Amstrong and Liviya James, "Behind the Wrapper: Greenwashing in the Chocolate Industry", *Mighty Earth* (December 2018), available at: http://www.mightyearth.org/wp-content/uploads/Chocolate-Report_english_FOR-WEB.pdf.
[978] Report for Fern, Tropenbos International and Fairtrade, authored by Duncan Brack, "Towards sustainable cocoa supply chains: Regulatory options for the EU" (June 2019), available at: https://www.fern.org/news-resources/towards-sustainable-cocoa-supply-chains-regulatory-options-for-the-eu-1978/.

child labour and deforestation, and a number of EU Member States have announced programmes to address the sustainability of the cocoa sector.

> There is increasing acknowledgement, however, that while these current initiatives have had some positive impacts, they have not succeeded, and are not likely to succeed, in tackling low prices and poverty, child labour, deforestation and illegality across the whole cocoa sector.

Similarly, in the garment sector, a recent report showed that voluntary initiatives are failing to deliver living wage.[979] The report assessed 32 leading brands (from luxury, sportswear, fast fashion and online retail sectors) and found that, whilst 84% of brands had made some sort of commitment to wages being enough to meet worker's basic needs, very few were actually following through on this commitment in any measurable way, and none could yet give evidence showing that any worker in their supply chains are being paid a living wage.

In its resolution on the EU flagship initiative on the garment sector, the European Parliament noted:

> [H]ow the existing voluntary initiatives for the sustainability of the garment sector's global supply chain have fallen short of effectively addressing human rights and labour rights-related issues in the sector; calls on the Commission, therefore, to go beyond the presentation of a Staff Working Document and to propose binding legislation on due diligence obligations for supply chains in the garment sector.[980]

In relation to deforestation, a recent report from ClientEarth and Global Witness noted that:[981]

> Not one of the 500 main companies and financial institutions in forest-risk supply chains is on track to eliminate commodity-driven deforestation from their supply chains and portfolios by 2020. Yet, nearly half have made commitments to do so by 2020 or earlier.

In relation to climate change, a recent report of the Special Rapporteur on extreme poverty and human rights warned against an overreliance on voluntary, private sector efforts:[982]

> There is little doubt that companies will play a role in providing and implementing solutions to climate change, but an overreliance on voluntary, private sector efforts would be a mistake. Climate change is a market failure, and voluntary emissions reduction commitments will only go so far. As of May 2019, 554 companies had committed to reductions in greenhouse gas emissions as a part of the 'Science Based Target Initiative', but the initiative is essentially toothless and relies entirely on self-reporting.

The report further adds that:[983]

> [I]t is clear that corporate actors cannot and will not, of their own accord, be capable of promoting a comprehensive approach that ensures the sort of

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[979] Labour Behind the Label, "Tailored Wages UK 2019: The state of pay in the global garment industry", available at: http://labourbehindthelabel.org/tailoredwagesuk2019/.
[980] European Parliament resolution of 27 April 2017 on the EU flagship initiative on the garment sector (2016:2140(INI)).
[981] ClientEarth and Global Witness, above n 814 at 5.
[982] UN Human Rights Council, "Report of the Special Rapporteur on extreme poverty and human rights: Climate change and poverty", A/HRC/41/39 (17 July 2019) at para 48.
[983] Ibid at 69.

economic and social transformation that climate change mitigation demands. Through the actions of the fossil-fuel industry in particular, and highly successful corporate lobbying to downplay or ignore climate change in many countries, the private sector has demonstrated its inability to take any sort of leadership role in climate change mitigation. This is true even though companies and major investment funds are now acutely aware of the upheavals on the horizon. The result is that governments, individually and collectively, need to take responsibility for implementing a comprehensive transformative program aimed at mitigation.[984]

The UNGPs call on States to consider "a smart mix of measures" at national and international level, combining mandatory and voluntary measures, to foster business respect for human rights.[985]

5.3 New regulation requiring due diligence reporting (Option 3)

This option would entail new regulation at EU level requiring companies to report publicly on the steps they have taken to identify, address, prevent and mitigate any adverse human rights and environmental impacts in their own operations or of third-party business relationships (including in the supply chain).

Reporting requirements do not in themselves require a substantive due diligence standard. Where they are enforceable, enforcement usually relates to the adequacy of the frequency or content of the report, rather than whether the processes which were reported meet a certain standard. Reporting requirements do not usually provide remedies to those affected.

Regulation which requires due diligence reporting already exists at EU level in the form of the EU Non-financial Reporting Directive. Another prominent example of a reporting requirement on due diligence referenced by several stakeholders is the UK Modern Slavery Act.

Many of the reporting requirements discussed in this study do not impose an effective sanction for the failure to report. Examples include the UK Modern Slavery Act, which was mentioned by several stakeholders across the EU as a model of this type of reporting regulation. Where corporate compliance of these kind of reporting requirements are evaluated, the focus tends to be on whether a report has been provided, rather than on the content and veracity of the report.[986]

However, more recent reporting requirements do envision enforcement of reporting requirements. For example, the EU Non-Financial Reporting Directive states:[987]

> Member States should ensure that effective national procedures are in place to enforce compliance with the obligations laid down by this Directive, and that those procedures are available to all persons and legal entities having a legitimate interest, in accordance with national law, in ensuring that the provisions of this Directive are respected.

However, this enforcement would relate to compliance *with the reporting requirement*: whether a report was produced, whether it was adequate to meet the criteria of the

[984] Ibid at 18.
[985] Commentary to UNGP 3.
[986] Bhumann, above n830 at 29.
[987] EU Non-Financial Reporting Directive, above n900 at para 10 of the Preamble.

reporting requirement, and whether it was accurate.[988] For example, the EU NFRD states:[989]

> Statutory auditors and audit firms should only check that the non-financial statement or the separate report has been provided. In addition, it should be possible for Member States to require that the information included in the non-financial statement or in the separate report be verified by an independent assurance services provider.

In accordance with this, the EU NFRD provides:[990]

> Member States shall ensure that the statutory auditor or audit firm *checks whether* the non-financial statement referred to in paragraph 1 or the separate report referred to in paragraph 4 *has been provided*.
> …
> Member States *may* require that the *information* in the non-financial statement referred to in paragraph 1 or in the separate report referred to in paragraph 4 *be verified* by an independent assurance services provider. [Our emphasis]

The reporting requirement does not in itself constitute a duty to undertake due diligence. Therefore, even where there is oversight of the frequency, detail and veracity of the report, as set out above, this is still not an enquiry into whether the company undertook the due diligence *which was reasonably required* under the circumstances. Reporting requirements in themselves generally do not provide for legal liability for a failure to meet a standard of care, regardless of whether harms are reported, or failed to be reported.

In addition, reporting requirements provide no access to remedy for those who have been affected by the harms. In other words, even when reporting requirements are enforced, and information contained in reports verified, the existence or absence of a compliant report will not provide those affected with a remedy.

Moreover, reporting requirements, even when they expressly apply to harms external to the company, are by their nature focused on the provision of information relating to the "material risks" for the performance of the company.[991]

Concerns have been raised about the effectiveness of reporting requirements. A recent report for the Netherlands government on responsible business conduct found that the assumption that companies will be eager to comply with reporting regulation due to

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988 For example see the UK Country Report: "[T]he Financial Conduct Authority has the power to impose large fines on listed companies that fail to publish information likely to have a significant effect on the price of financial instruments (e.g. shares) on a timely basis. Although no fines levied by the Financial Conduct Authority to date concern non-disclosure of information relating to a company's involvement in human rights issues, it follows that human rights issues which lead to losses or the impairment of assets (e.g. where community or labour protests halt production or operations) this would need to be publicly disclosed. The Financial Conduct Authority can also impose fines on listed companies which fail to comply with the Disclosure Guidance and Transparency Rules when making statutory filings; e.g. the requirement to describe the company's 'principal risks and uncertainties'…" [References omitted here, see UK Country Report].
989 Para 16 of the Preamble of the EU NFRD.
990 Art 19a (5) and (6) of the EU NFRD.
991 For example see the UK Country Report: "Complaints lodged by an NGO with the Financial Conduct Authority and the Financial Reporting Council in 2018 against certain listed companies for alleged failures to set out and particularise climate change related risks in their statutory filings may set an interesting precedent for similar human rights focussed complaints. This kind of activism may lead directors to apply greater attention to the identification and management of potential human rights issues by companies, although to some extent this may depend on the complainants successfully showing that specific human rights issues (e.g. labour welfare issues in the supply chain) are a material concern for shareholders (evidenced by shareholder resolutions, for example). Whilst directors are obliged under section 172 of the Companies Act 2006 to have regard to employees, the community and the environment in carrying out their functions, this is ultimately within the context of a broader fiduciary duty to promote the success of the company for the benefit of the members as a whole. In other words, the company's (and shareholders') interests have primacy. However, recognising that the more severe human rights issues can have '*reputational, financial or legal'* repercussions, a failure to carry out human rights due diligence (which is appropriate given the business's operating context and relevant severe human rights risks) may mean a company's directors are poorly positioned to report on material risks to the company". [References omitted here; see UK country report]

pressure faced from civil society, consumers and investors is "not confirmed by evaluative research".[992]

For example, in relation to the California Act, a 2015 Report finding found that only 15% of companies required to report under the Act were fully compliant.[993] In relation to the UK Modern Slavery Act, the Home Offices estimates that 40% of companies covered by the legislation have failed to publish a statement.[994] The Independent Review of the UK Modern Slavery Act concluded that, despite the Act's contribution to raising awareness of slavery and human trafficking in supply chains, the impact of the legislation has been limited to date.[995] The report states:[996]

> [E]vidence gathered by our Expert Advisers shows that there is a general agreement between businesses and civil society that a lack of enforcement and penalties, as well as confusion surrounding reporting obligations, are core reasons for poor-quality statements and the estimated lack of compliance.

The Business and Human Rights Resource Centre has tracked and assessed the transparency statements of the largest companies in the UK (FTSE 100) since the adoption of the UK Modern Slavery Act. In its 2018 report, it found that the legislation "has failed to deliver the transformational change many hoped for". In particular, the report highlighted that:

> [T]hree years on, most companies still publish generic statements committing to fight modern slavery, without explaining how. Sadly, only a handful of leading companies have demonstrated a genuine effort in their reporting to identify and mitigate risks.[997]

Similar conclusions have been drawn in relations to the limited impact of the EU Non-Financial Directive. The 2018 Alliance for Corporate Transparency analysed the implementation of the EU Non-Financial Reporting Directive in the reports of 105 companies from three sectors (information and communication technologies, healthcare, and energy and resource extraction).[998] The report examined the description of policies and due diligence processes, outcomes, principal risks (including with respect to business relationships) and key performance indicators (KPIs) and to examine if the disclosed information was specific enough to allow understanding of the companies' impact and strategy.[999] The report found that, if over 90% of companies express commitment to respect human rights, only 36% describe their due diligence processes.[1000] According to the report, a majority of companies do not provide any information that would allow a stakeholder to understand how their commitment to respect human rights is put into practice:[1001]

> The vast majority of companies acknowledge in their reports the importance of environmental and social issues for their business. However, in only 50% of cases for environmental matters and less than 40% for social and anti-corruption

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992 PWC, above n 830 at 59.
993 Development International, "Corporate Compliance with the California Transparency in Supply Chains Act of 2010" (2 November 2015). See also https://www.theguardian.com/sustainable-business/2016/jan/22/california-anti-slavery-law-development-international-sun-maid-asia-human-trafficking.
994 UK Home Office, "Home Office tells business: open up on modern slavery or face further action" (18 October 2018), available at: https://www.gov.uk/government/news/home-office-tells-business-open-up-on-modern-slavery-or-face-further-action.
995 Field, Miller and Butler-Sloss, above n830.
996 Business & Human Rights Resource Centre, "FTSE 100 & the UK Modern Slavery Act: From Disclosure to Action", available at: https://www.business-humanrights.org/sites/default/files/FTSE%20100%20Briefing%202018.pdf.
997 Ibid at 8.
998 Alliance for Corporate Transparency Project, "2018 Research Project: The state of corporate sustainability disclosure under the EU Non-Financial Reporting Directive", available at: http://www.allianceforcorporatetransparency.org/assets/2018_Research_Report_Alliance_Corporate_Transparency-66d0af6a05f153119e7cffe6df2f11b094affe9aaf4b13ae14db04e395c54a84.pdf at 7.
999 Ibid.
1000 Ibid at 6.
1001 Ibid at 8.

matters, this information is clear in terms of concrete issues, targets and principal risks.

The general information that most companies provide does not allow readers to understand their impacts and by extension their development, performance and position, as required by the NFR Directive.

The report further stated that:

With respect to climate change, the biggest gaps in the current practice are the lack of reporting by companies in the Energy and Resource Extraction sector on both short and long time horizons and the transition to a below 2°C scenario, which are mentioned by 26% and 21% of companies respectively.

Also, Karin Buhmann has noted, in relation to the EU Non-Financial Reporting Directive, that, the operative articles of the Directive predominantly focus on ex-post measures, neglecting ex-ante organisational and proactive due diligence necessary to prevent the human rights and environmental harm from taking place in the first place.[1002]

In another example, although the UK Modern Act makes provision for the Secretary of State to seek an injunction when a company fails to issue the statement,[1003] this has not been used in practice and there have so far been no penalties for non-compliance.[1004] Like with the California Act, issues of non-compliance have been reported to be widespread with the UK Modern Slavery Act.[1005] The UK Modern Slavery Act was independently reviewed during 2019 and it was noted that:[1006]

While it has contributed to greater awareness of modern slavery in companies' supply chains, a number of companies are approaching their obligations as a mere tick-box exercise, and it is estimated around 40 per cent of eligible companies are not complying with the legislation at all.

The review made recommendations for stronger provisions to ensure compliance and improve the quality of modern slavery statements produced by eligible companies.[1007] In particular, the review stated that:[1008]

Stakeholders were clear that the lack of clarity, guidance, monitoring and enforcement in modern slavery statements needed to be addressed to increase compliance and quality. We agree and recommend that companies should not be able to state they have taken no steps to address modern slavery in their supply chains, as the legislation currently permits, and that the six areas of reporting currently recommended in guidance should be made mandatory. We also recommend that Government should set up a central repository for statements; that the Independent Anti-Slavery Commissioner should monitor transparency; sanctions for non-compliance should be strengthened; and that Government should bring forward proposals for an enforcement body to enforce sanctions against non-compliant companies. A requirement for greater transparency from business is becoming usual practice, with businesses required to report on a number of issues, including for example their gender pay gap. It is only right that reporting on modern slavery should be taken equally seriously.

[1002] Bhumann, above n830 at 38.
[1003] UK Modern Slavery Act 2015 (UK MSA), s.54(11).
[1004] Field, Miller and Butler-Sloss, above n839 at para 15.
[1005] NYU Stern Center for Business and Human Rights, above n837 at 5.
[1006] Field, Miller and Butler-Sloss, above n839 at para 15.
[1007] Ibid at para 16.
[1008] Ibid at para 17.

Virginia Mantouvalou discusses the approach of the UK Modern Slavery Act. Although this Act provides for criminal sanctions for domestic offences of slavery, the transparency provision which requires reporting about due diligence in the supply chain does not provide for a sanction:[1009]

> In contrast to the criminalisation of modern slavery found in the early sections of the MSA, when it comes to business conduct we find a soft law provision. The MSA did not attempt to pierce the corporate veil with hard legal rules and sanctions for non-compliant businesses. Instead, it included section 54, entitled 'Transparency in Supply Chains etc', which imposes a duty on businesses to have transparency in their supply chains with respect to slavery and human trafficking.

Mantouvalou continues about the reporting requirements of the UK Modern Slavery Act:[1010]

> There are shortcomings both in the design of the system under section 54 and its implementation. At a general level, it is questionable whether self-regulation alone is the best way to deal with business misconduct. The role of reflexive law in labour law has been questioned in scholarship, especially where workers' human rights are in issue. Particularly in relation to the regulation of business conduct, selfregulation has been criticised for simply protecting businesses from reputational damage and for limiting their liability, and has been shown through empirical research to be ineffective unless combined with strong public institutions and laws.

Genevieve LeBaron and Andreas Rühmkorf undertook a study which compares how companies implement the UK Modern Slavery Act to how companies implemented the UK Bribery Act (which provides for state-based oversight and enforcement, including criminal sanctions.) They write:[1011]

> That the Modern Slavery Act fails to establish new public labour standards or enforcement mechanisms is significant, given the differences we observe between company policies and practices on bribery and forced labour. While stringent legislation appears to strengthen private governance, such as by spurring lead firms to use their contractual bargaining power and implementation of due diligence based procedures, less stringent legislation does not appear to spur change in company practices. This variation is understandable, given that the Bribery Act model provides an incentive for companies to avoid sanctions by implementing adequate due diligence procedures, while the Modern Slavery Act does not impose additional requirements (except in regards to reporting) and carries no sanction for non-compliance. Within the Modern Slavery Act, the substitution of a vague reporting requirement over a more stringent model of public governance appears to have undermined its effectiveness in 'steering' corporate behaviour. Although it is possible that company strategy could still evolve, we are sceptical that this legislation will result in meaningful changes to company and supplier policies on forced labour, given the shortcomings we have documented in its institutional design.

As a result of these limitations, the recent above-mentioned report for the Netherlands government on responsible business conduct recommends that "new instruments and

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[1009] Virginia Mantouvalou, "The UK Modern Slavery Act 2015 Three Years On" (2018) 81:6 *The Modern Law Review* 1017 at 1038.
[1010] Ibid at 1040.
[1011] LeBaron and Rühmkorf, above n830 at 26.

strategies should encourage, promote and enforce the implementation or all steps of the due diligence cycle, as opposed to focusing solely on reporting".[1012]

However, it has been argued that reporting laws have played a role in raising awareness internally within companies about human rights and environmental due diligence.[1013] Those laws that require Board members to sign off have in particular been said to drive internal conversations about the company's due diligence for its impacts.[1014] Moreover, as these laws are fairly new, company laws relating to corporate reporting generally may increasingly be used by corporate regulators to enforce non-financial reporting requirements.

5.4 New regulation requiring mandatory due diligence (Option 4)

A mandatory due diligence requirement at EU level would require companies to carry out due diligence to identify, prevent, mitigate and account for actual or potential human rights and environmental impacts in its own operations or supply chain.

The due diligence process is understood as an ongoing, context-specific process which includes the following components:

1) Identifying and assessing actual and potential impacts
2) Integrating and acting upon the findings
3) Tracking the effectiveness of these actions, and
4) Communicating how impacts are addressed, including through reporting.

In line with the UNGPs, the OECD Guidelines and the ILO MNE declaration, the due diligence process should include meaningful consultation and collaboration with potentially affected and other relevant stakeholders (including civil society organisations, workers' organisations, and investors) along the value chain.

This duty would require companies to meet a certain standard of care of due diligence for the human rights and environmental impacts in their own operations and supply chains (or value chains).

In accordance with legal understanding of due diligence, this standard of care would allow for a company to demonstrate, in its defence, that it has met this standard by undertaking the required level of due diligence.

The terminology of the standard could take different forms. For example:

- The duty could be phrased as, for example, a duty to exercise due diligence of care, a duty of vigilance or a duty to prevent human rights and environmental harms.

- The required level of due diligence which the company would need to demonstrate in its defence to escape liability could be phrased as, for example, adequate due diligence, appropriate due diligence, or reasonable due diligence.

This duty to exercise due diligence as a standard of care could be incorporated in company law, but would be context-based (similar to a tort standard) in that it would require the *due* diligence which is "due" or required in the specific circumstances.[1015] Factors which would be determinative in deciding whether the diligence met this standard would include:

[1012] PWC, above n830 at 61.
[1013] For example, see Landau, above n865.
[1014] See Section 2 Market Practices.
[1015] Nicolas Bueno writes about the Swiss Popular Initiative: "Concretely, the introduction of a mandatory due diligence provision objectifies the expected conduct that Switzerland-based companies must apply with a view to preventing adverse human rights and environmental impacts in Switzerland and abroad. In this regard, the text of the initiative does not

- The severity[1016] or significance[1017] of the impact
- The size of the company
- The sector
- The operational context
- The ownership and structure of the company
- The resources of the company
- The standards and practices applicable within the industry (including any sector-specific guidance on due diligence)
- The level of leverage which the company has, and whether this was exercised.

For the above determination it will be relevant what the company knew or *ought to have known* under the circumstances.

The due diligence duty of care is focused on the risks external to the company, i.e. the *risks to people or the planet*. In this way, due diligence as a corporate standard of care differs from fiduciary duties which director owe to the company, in that the duty does not (only) relate to risks that are material *to the company* or in the company's interest to address. The due diligence duty of care relates to external human rights and environmental harms which the company is causing, to which it is contributing or directly linked, *regardless* of whether it is in the company's (short or long-term) interest to consider these risks:[1018]

> Human rights due diligence can be included within broader enterprise risk management systems, provided that it goes beyond simply identifying and managing material risks to the company itself, to include risks to rights-holders.

In accordance with the concept of due diligence, this defence would also allow for prioritisation of some risks over others. The concept of due diligence as described in the UNGPs and other standards is based on the acknowledgement that companies do not have unlimited resources and may therefore need to prioritise those risks which they identify as the most "severe",[1019] the "most significant",[1020] or the most "salient"[1021] (terminology used by the UNGPs Reporting Framework).[1022] Severity is defined with reference to the scale, scope and irremediable character of the impact. The assessment and determination of severity would need to be proved by the company in order to justify its prioritisation.[1023]

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distinguish between the three scenarios presented above: causing an adverse impact, contributing to an adverse impact through the enterprise's own activities, and adverse impacts directly linked to the enterprise's operations by a business relationship. It broadly states that due diligence 'duties apply to controlled companies as well as to all business relationships'. However, according to the explanation of the initiative text, section (2)(b) introduces a mandatory due diligence provision based on the UNGP and the OECD Guidelines for Multinational Enterprises. Therefore, the international framework may provide guidance on how to interpret the text of the initiative. Although not expressly referenced in the text, this standard of conduct should help to identify whether a company has committed a fault and should be held liable for its own actions and omissions on the basis of the general tort of negligence." Nicolas Bueno, "The Swiss Popular Initiative on Responsible Business: From Responsibility to Liability", in Liesbeth Enneking et al (eds.), A*ccountability, International Business Operations, and the Law*, London: Routledge (2020), 239.

[1016] UNGP 17(b) which states that human rights due diligence "will vary in complexity with the size of the business enterprise, the risk of severe human rights impacts, and the nature and context of its operations".

[1017] OECD, above n848, Chapter II, Commentary, para 16: "Where enterprises have large numbers of suppliers, they are encouraged to identify general areas where the risk of adverse impacts is most significant and, based on this risk assessment, prioritise suppliers for due diligence."

[1018] Commentary to UNGP 17.

[1019] Above n 1016.

[1020] OECD, above n848, Chapter II, Commentary, para 16: "Where enterprises have large numbers of suppliers, they are encouraged to identify general areas where the risk of adverse impacts is most significant and, based on this risk assessment, prioritise suppliers for due diligence."

[1021] UN Guiding Principles Reporting Framework with implementation guidance, available at: https://www.ungpreporting.org/wp-content/uploads/UNGPReportingFramework_withguidance2017.pdf at 22, which defines salient human rights issues at "those human rights that are at risk of the most severe negative impact through its activities of business relationships".

[1022] UN Guiding Principles Reporting Framework, available at: https://www.ungpreporting.org/wp-content/uploads/UNGPReportingFramework_2017.pdf.

[1023] It is also noted that these terms and the prioritisation principle seem to be firmly understood, as they were mentioned in the Market Practices section by stakeholders across the spectrum.

The duty would be a substantive legal duty rather than a procedural requirement. The enquiry into whether the standard of care was met would take into account all of the following:

- Which processes or steps were put in place
- Whether these steps were adequate / reasonable / appropriate in the particular circumstances, taking into account the relevant context and the risks (including what the company ought to have known)
- Whether the process was implemented; and
- How it was implemented in practice.

In this way, a company will not be able to defend itself by simply "ticking the boxes" or undertaking a process which is titled as "due diligence", in line with the UNGPs which make clear that the conducting due diligence should not be an automatic defence.[1024] The enquiry will go further to evaluate whether these steps met the standard which were required in the particular circumstances. In our interviews and in the survey, stakeholders have expressed strong support for this wide and general understanding of due diligence, and indicated that this is essential in order for the same general standard to be applicable to all companies, in all sectors, in all circumstances. The open-ended nature of the standard allows it to be applicable into the finest detail, on the facts of a specific case, and also taking into account the relevant industry standards and factual circumstances of what the company has been doing about the issue.

The UN Human Rights Council noted that the exercise of human rights due diligence could be a basis for a possible defence to liability in some cases. The UN Human Rights Council added that:[1025]

> The equitability and rights-compatibility of permitting such a defence will depend on many factors, including what kind of harm was involved, the connection of a company to the harm, victims' alternative avenues to remedy, and the State's regulatory aims.

The UN Human Rights Council concluded that:[1026]

> Permitting a defense to liability based upon human rights due diligence activities could incentivize companies to meaningfully engage in such activities and have important preventative effects…

The report noted, however, that a due diligence defence would lead to concerns of "inappropriateness and unfairness" if it would allow for "business enterprises seeking to raise due diligence defenses in cases where superficial "check box" approaches to human rights due diligence might be used as a reference point instead of genuine attempts to identify, mitigate, and address human rights risks as contemplated in the UNGPs." The report highlighted "the importance of ensuring that judges are familiar with the content of the UNGPs as it relates to human rights due diligence so they can distinguish genuine efforts by business enterprises to identify and address risks from superficial efforts, and make their decisions accordingly."[1027] This point ties in with the discussion below on non-binding guidance which could accompany the regulation to inform judges, companies, regulators, communities and other stakeholders of the details relating to its implementation.

[1024] Commentary to UNGP 17.
[1025] UN Human Rights Council, above n850 at para 25.
[1026] Ibid at para 29.
[1027] Ibid at para 29.

Given the importance of this option in terms of the mandate of this study, we have subdivided this regulatory option into three sub-options:

- Sub-option 4.1: New regulation applying to a narrow category of business (limited by sector)
- Sub-option 4.2: New regulation applying horizontally across sectors
- Sub-option 4.3: Sub-options 1 and 2 accompanied by a statutory oversight and enforcement mechanism.

They are elaborated in the following.

Sub-option 4.1: New regulation applying to a narrow category of business (limited by sector)

This sub-option would entail a substantive legal duty to meet a standard of due diligence, as described above, but it would only apply to a narrow category of business, for example, a certain sector or commodity. Some sectoral due diligence requirements already exist, including the above-mentioned EU-level requirements in the timber, agriculture and conflict minerals context. However these require a hybrid of reporting and substantive action, and do not offer remedies for victims. For example:

The EU timber regulation (EUTR)[1028] requires operators to exercise due diligence throughout the supply chain in order to ensure that they are not placing illegally harvested timber and products derived from such timber on the EU market. Competent authorities nominated by EU Member States[1029] are responsible for enforcing the Regulation and setting the penalties in case of non-compliance.

The 2016 Report on the first two years of implementation of the EUTR revealed that the Regulation had had some positive effects, notably in terms of raising awareness of the problem of illegal logging amongst EU consumers,[1030] and added "significant value to the international efforts to halt deforestation and forest degradation, conserve biodiversity and address climate change".[1031] The report also noted that EU operators were gradually taking steps to ensure the legality of their suppliers. In particular, the report noted in relation to the exercise of due diligence [DD] by operators that:[1032]

> Operators across the EU have not consistently implemented the DD requirements during the first two years of application of the Regulation. Although evidence shows that the situation is gradually improving, the overall compliance by the private sector remains uneven and insufficient.

The report further stated that:[1033]

> Although the uptake of the DD obligation has been slow, there is evidence that operators are gradually implementing DD, demanding more information and legality assurance from their suppliers. This demonstrates that the DD obligation has the potential to change market behaviours of operators, thus creating supply chains free of illegally harvested timber. However, more time is needed before a definitive assessment can be made.

[1028] Regulation (EU) No 995/2010, above n862.
[1029] The list of Nominated Competent Authorities can be found here: http://ec.europa.eu/environment/forests/pdf/list_competent_authorities_eutr.pdf.
[1030] Report from the Commission to the European Parliament and the Council, Regulation (EU) No 995/2010 of the European Parliament and of the Council of 20 October 2010 laying down the obligations of operators who place timber and timber products on the market (the EU Timber Regulation), COM(2016) 74 final, at para 5.4.
[1031] Ibid at para 5.1.
[1032] Ibid at para 5.4.
[1033] Ibid at para 5.4.

It was further found that uneven implementation and patchy enforcement did not help establish a level playing field and more effort was needed from both the Member States and the private sector to ensure its effective and efficient application.[1034]

The 2017 Report on the implementation of the EUTR noted that clear progress had been made and that the number of checks made and sanctions applied for violations of the EUTR had significantly increased.[1035] However, the report also underlined that "continuous efforts are needed to ensure a uniform and effective application of the EUTR across countries" since "uneven implementation can have potential implications in terms of both the effectiveness of legislation and a level playing field for market operators".[1036]

The EU conflict minerals regulation[1037] requires EU-based companies that import four minerals - tin, tantalum, tungsten and gold - from conflict-affected and high-risk areas into the EU to exercise due diligence by checking that what they buy is sourced responsibly and does not contribute to conflict or other related illegal activities. Each Member State is tasked to designate one or more competent authorities responsible for the oversight of the Regulation.[1038] In case of non-compliance, Member State competent authorities shall issue a notice of remedial action to be taken by a Union importer. However, the regulation does not provide for penalties in the case of non-compliance with a notice of remedial action.[1039] The regulation will enter into force on 1 January 2021.

It is noted that due to the mandate of this study, which is focused broadly on human rights and environmental due diligence within the sustainability agenda, the regulatory options considered do not focus on **issue-specific regulation** such as those particular to modern slavery or child labour. It may nevertheless be helpful to note that similar concerns apply to regulation which is limited in scope to specific issues as to limitation by size. It has been argued that one of the unintended effects of the approach focusing on one single issue, such as modern slavery, child labour or conflict minerals, is that it detracts the attention from other types of impacts or other serious breaches of human rights.[1040] This disincentivizes broader due diligence as it "creates a strong driver for businesses to prioritise efforts to address that particular issue, even if, objectively, it would not qualify as one of the salient human rights risks facing the organisation".[1041]

Also, due to the various examples of existing issue-specific regulation, and in order to inform a broad understanding of survey perceptions of current and possible future regulation mechanisms, survey respondents were nevertheless asked about issue-specific regulation. As evidenced in the Market Practices section, the majority of stakeholders indicated a preference for a due diligence regulation which would apply across "all EU-recognised human rights and environmental impacts".[1042]

Sub-option 4.2: New regulation applying horizontally across sectors

This regulatory option would apply the above-mentioned duty to carry out due diligence as a standard of care to companies operating in all sectors. We discuss this option with respect to three sub-options, namely as applicable only to large companies, applicable to all

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[1034] Ibid at para 7.
[1035] Report from the Commission to the European Parliament and the Council, Regulation (EU) No 995/2010 of the European Parliament and of the Council of 20 October 2010 laying down the obligations of operators who place timber and timber products on the market (the EU Timber Regulation), COM(2018) 669, at para 7.
[1036] Ibid at para 7.
[1037] Regulation (EU) 2017/821, above n861.
[1038] Ibid Article 10.
[1039] See SOMO, "European Commission urged to implement regulation on 'conflict minerals' properly" (26 April 2019), available at: https://www.somo.nl/european-commission-urged-to-implement-regulation-on-conflict-minerals-properly/.
[1040] Landau, above n 865.
[1041] GBI and Clifford Chance, "Business and Human Rights: Navigating a Changing Legal Landscape" (2019), available at: https://www.cliffordchance.com/briefings/2019/03/business_and_humanrightsnavigatingachangin.html.
[1042] See in this regard Market Practices section.

companies regardless of size, including SMEs, and a general duty applicable to companies of all sizes plus additional obligations for large companies.

Sub-option 4.2(a): applying only to a defined set of large companies:

This would entail a general legal duty to undertake due diligence, as described above, but would only apply to a certain defined set of large companies. Most of the laws discussed above only apply to certain large companies, defined either by turnover or number of employees. For example, the French Duty of Vigilance Law applies to French companies employing over 5000 in France (through their direct and indirect subsidiaries), or employing over 10 000 employees worldwide (through their direct or indirect subsidiaries). The UK Modern Slavery Act applies based on turnover. The Swiss counter-proposal excludes SMEs (unless they are operating in high risks sectors), as it applies to companies exceeding two of the following three thresholds: a balance sheet total of 40 million CHF/USD; a turnover of 80 million CHF/US, or 500 full-time employees.[1043] The EU non-financial reporting Directive applies to large public interest companies which employ more than 500 employees.[1044]

Sub-option 4.2(b): applying to all business, including SMEs

This would entail a legal duty to undertake due diligence, as described above, and it would apply to all companies, including SMEs. As discussed above, the UK Anti-Bribery Act applies to all companies including SMEs. A study by the UK government found that two thirds (66%) of SMEs had knowledge of the Bribery Act and its legal liability implications, and that "perceived knowledge and understanding was greatest among those SMEs that were aware of corporate liability for failure to prevent bribery (79%) compared to those that had only heard of the Act itself (45%)".[1045]

The French Law on the Duty of Vigilance applies to a specific set of large companies only, thereby excluding SMEs. The Swiss legislative counter-proposal also applies to large companies and excludes SMEs, except those SMEs that operate in high risk sectors.[1046] If the proposal were to become law, high risk sectors are to be defined on a regular basis by the government.

The initial text of the Swiss Popular Initiative on Responsible Business applied to *all* Swiss-based companies, although it acknowledged that the needs of small and medium-sized companies that have limited risks of this kind are to be taken into account.[1047] The Dutch Child Labour Due Diligence Law also applies to all companies, and even extends to non Dutch-based companies supplying goods into the Netherlands.[1048]

In this respect, the Interpretive Guide to the Corporate Responsibility to respect human rights notes that:[1049]

[1043] Swiss Coalition for Corporate Justice, "How does the parliamentary counter-proposal differ from the popular initiative (RBI)", available at: https://corporatejustice.ch/wp-content/uploads/2018/07/Comparision_RBI_counter-proposal_EN-1.pdf.
[1044] It is estimated to cover approximately 6,000 large companies and groups across the EU, including listed companies, banks, insurance companies and other companies designated by national authorities as public-interest entities. See https://ec.europa.eu/info/business-economy-euro/company-reporting-and-auditing/company-reporting/non-financial-reporting_en.
[1045] HM Government, "Insight into awareness and impact of the Bribery Act 2010: Among small and medium sized enterprises (SMEs)" (2015), available at: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/440661/insight-into-awareness-and-impact-of-the-bribery-act-2010.pdf.
[1046] In the current counter-proposal the Swiss government will periodically define which sectors are deemed to be "high risk". This is potentially inconsistent with the UNGPs' understanding of due diligence, in that human rights risks are not sector-specific and all companies (even SMEs) need to decide for themselves whether their activities are high risk.
[1047] Swiss Coalition for Corporate Justice, "The Initiative Text with Explanations" https://corporatejustice.ch/wp-content/uploads//2018/06/KVI_Factsheet_5_E.pdf.
[1048] The Netherlands Child Labour Due Diligence Act 2019.
[1049] United Nations Office of the High Commissioner for Human Rights, "The Corporate Responsibility to Respect Human Rights: An Interpretive Guide" (2012) at 20.

> In many instances, the approaches needed to embed respect for human rights in a smaller enterprise's operations can mirror the lesser complexity of its operations. However, size is never the only factor in determining the nature and scale of the processes necessary for an enterprise to manage its human rights risks. The severity of its actual and potential human rights impact will be the more significant factor. For instance, a small company of fewer than 10 staff that trades minerals or metals from an area characterized by conflict and human rights abuses linked to mining has a very high human rights risk profile. Its policies and processes for ensuring that it is not involved in such abuses will need to be proportionate to that risk.

Recent civil society calls for mandatory human rights and environmental due diligence at EU level also expressly add a call for such regulation to apply to financiers and investors "who wield a huge amount of power in facilitating projects that can have large environmental and human rights impacts".[1050] In addition, they argue that it should apply to the public sector. In this respect, it is worth noting that the UK has issued a consultation on extending section 54 of the UK Modern Slavery Act to include the public sector.[1051]

Sub-option 4.2(c): general duty applying to all business plus specific additional obligations only applying to large companies

This sub-option was introduced by agreement with the Commission after the empirical research phase of the study had already closed, and so was not presented to stakeholders in this exact format.

It is a "mixed" option which enables a combination of obligations which are applicable to companies of all sizes with specific additional obligations only for large companies.

This sub-option is discussed with reference to one particular example of how this sub-option could be applied, namely "a general due diligence duty applying to all business, including SMEs, plus a specific obligation linked to Paris agreement aligned targets for specific large companies." This report contains a discussion of this sub-option specifically and exclusively with reference to the above example of how such a sub-option may be conceived with reference to the Paris Agreement.

The late introduction of this example of obligations linked to the Paris agreement on climate change was thought to be justified based on recent developments during early to mid-2019. These developments clarified ways in which the due diligence expected of individual companies could be utilised for due diligence for climate change impacts.

In particular, recent developments which justify the late inclusion of this sub-option are:

- The finding by the OECD National Contact Point in the Netherlands that a company's due diligence should include the setting of targets and measurable objectives for climate change, even in the absence of agreed international standards for such measurements.[1052]

- The August 2019 ruling, by the Polish District Court of Poznán, that the decision of the Polish energy company Enea to authorise construction of a coal power plant

[1050] ClientEarth and Global Witness, above n 814 at 3.
[1051] James Butler, "Government is proposing to extend the Modern Slavery Act to the public sector. Let's help them make it easy to do by supporting the consultation" (12 July 2019), available at: https://party.coop/2019/07/12/extending-modern-slavery-act-to-the-public-sector/.
[1052] The Netherlands National Contact Point for the OECD Guidelines for Multinational Enterprises, *Oxfam Novib, Greenpeace Netherlands, BankTrack and Friends of the Earth Netherlands (Milieudefensie) versus ING*, Final Statement, 19 April 2019, available at: https://www.oecdguidelines.nl/documents/publication/2019/04/19/ncp-final-statement-4-ngos-vs-ing.

was legally invalid by reason of the unjustifiable financial (climate-related) risks to their shareholders.[1053]

- The publication of the EU Non-Binding Guidelines on corporate climate-related information reporting,[1054] which accompanies the EU non-financial reporting directive on the issue of climate change reporting.

In terms of this sub-option, it is noted that a general duty of due diligence applicable to all companies including SMEs would already include a duty to identify, assess, address, monitor and communicate on actions taken by the company with respect to its impacts on climate change. However, the "additional" requirements referred to in this sub-option would be applicable to all relevant large companies, regardless of their specific climate change risks.

Although the Paris Agreement does not set out specific due diligence requirements for companies, the above-mentioned statement of the Dutch NCP in the *ING* case[1055] is indicative of how this duty could be applied with reference to the due diligence requirements of the OECD Guidelines. In accordance with the findings of the NCP, any such "additional" measures could entail requirements relating to target-setting, measuring, and reporting relating to such actions.

In this respect, it is also noted that the proposed EU Regulation on disclosures relating to sustainable investments and sustainability risks would require financial market participants to report on information with:[1056]

> [R]eference to the adherence to responsible business conduct codes and internationally recognised standards for due diligence and reporting and, where relevant, *the degree of alignment with the long-term global warming targets of the Paris Climate Agreement*. [Our emphasis]

Sub-option 4.3: Sub-options 1 and 2 accompanied by a statutory oversight and enforcement mechanism

As noted throughout the report, many stakeholders have highlighted the importance of having robust enforcement mechanisms in place in order to ensure compliance with the regulation and thereby foster its effectiveness. These sub-options consider the legal implication of a failure to comply with either sub-option 1 or 2, and the possible liability and enforcement that might ensue.

Sub-option 4.3(a): mechanisms for judicial or non-judicial remedies

This option would provide for those affected by the company's failure to exercise due diligence to have access to judicial and/or non-judicial remedies. Some examples of remedies include the following:

- Remedies as financial compensation for the harm suffered
- Remedies as a restoration to the position before the harm took place, such as an order to clean up environmental damage.

[1053] ClientEarth, "Court win in world-first climate risk case puts future of Ostrołęka C coal plant in question" (2019), available at: https://www.clientearth.org/press/court-win-world-first-climate-case-ostroleka-c-future-in-question/.
[1054] European Commission, "Guidelines on reporting climate-related information", available at: https://www.eticanews.it/wp-content/uploads/2019/06/190618-climate-related-information-reporting-guidelines_en-1.pdf. See also: https://europa.eu/rapid/press-release_IP-19-3034_en.htm.
[1055] The Netherlands National Contact Point for the OECD Guidelines for Multinational Enterprises, above n1052.
[1056] Proposed EU Regulation on disclosures relating to sustainable investments and sustainability risks, above n973, Art 3gamma 2(d).

- Remedies as pecuniary damages, which are a way of quantifying the harm suffered in monetary terms.
- Preventative remedies could include injunctions or interdicts to force the company to cease with ongoing or potentially harmful conduct.
- In climate change actions, remedies could be compensation calculated as a percentage of the company's contribution to the damage.[1057]

In the human rights context, remedies can often be very innovative (such as an apology), but they need to be a remedy *for the victim.*

It is noted that a corporate fine which goes to the public purse and not to the victim therefore does not constitute a remedy. The UNGPs expect companies to remedy the adverse impacts which they cause or to which they contribute, but not those to which they are directly linked – which may, depending on the level of control they have over suppliers, include certain sections of the supply chain. To date, the French Duty of Vigilance law is the only example in this area which provides for a civil right of action in case the non-compliance with the due diligence requirements gave rise to a damage. People affected by the company's failure to implement a vigilance place are able to sue the company for compensatory damages.

A recent report for the European Parliament highlighted that an EU level legislation on mandatory due diligence with a civil liability element attached to it, modelled on the French law, would help improve access to justice for victims of corporate human rights abuses in third countries.[1058]

Sub-option 4.3(b): state-based oversight body and sanction for non-compliance

Oversight and enforcement bodies (often called administrative bodies) can be created at EU or Member State level. Oversight bodies could be established within existing state departments (such as the Departments of Justice and Trade) or new bodies could be created (such as the statutorily-created Modern Slavery Commissioners in the UK and Australia).

Where regulation is introduced in company law, the relevant oversight body could be the same entity responsible for the oversight of traditional corporate law requirements, such as those relating to the filing of annual reports, audits and number of directors. Where criminal mechanisms are introduced, oversight may take place by existing or newly created law enforcement bodies at domestic level.

Enforcement mechanisms could include fines, the appointment of monitors, withdrawal of licences or trade concessions, or even the dissolution of the company. At national level, state-based enforcement may include criminal sanctions, including prison sentences for individuals (such as directors or compliance officers). For example, the anti-bribery legislation (UK Bribery Act and US FCPA) discussed above is enforced through state-based oversight mechanisms. They provide for fines for the company, as well as individual criminal liability for the directors. The German draft outline for a suggested mandatory human rights and environmental due diligence law which has been discussed amongst stakeholders would also be enforced through state-based oversight mechanisms.

[1057] For instance, in the civil proceedings brought in Germany against RWE, the claimant, a Peruvian farmer, argued that RWE, as one of the world's top emitters of greenhouse gases, was partly responsible for the flooding risk to his house as it significantly contributed to global greenhouse gas emissions, and thus to climate change and that the company should therefore contribute its share (proportional to its historic CO_2 emissions) to the cost of protecting the claimant's house and the village of Huaraz from the risk of flooding due to the melting of two glaciers into a lake. At the moment of writing, the case is pending. For more information on the case, see Marx, Bright and Wouters, above n826 at 73.
[1058] Marx, Bright and Wouters, ibid.

Depending on what kind of body receives the oversight mandate, this sub-option could presumably have significant resource implications for the state.[1059] The supervision and enforcement of a due diligence requirement by the state would probably go very substantially beyond the current expertise, resources and legal mandate of national authorities responsible for supervising and enforcing corporate reporting requirements. Given the scope of what would need to be overseen, adequate resourcing of such an oversight body could be challenging. However, oversight mechanisms and state-based enforcement mechanisms have been found to be effective even where they are criticised for lacking enough resources and bringing very few prosecutions, such as the UK Anti-Bribery Act.[1060]

However, it is noted that despite potentially being more effective to change corporate behaviour, a sanction and a fine, or even a prison sentence or a dissolution of the company, *does not constitute a remedy* for the victim.

Enforcement through company law

As set out above, the legal basis for the regulatory intervention would relate to the regulation of corporate behaviour, and would therefore be most suitable within company law.

Companies are statutory creations which would not exist if it were not for their creation through company law provisions. Corporate law by definition is a body of law which regulates corporate behaviour. A regulation which creates corporate duties relating to the management of harms caused by corporate behaviour is therefore best placed within the framework of corporate law.

This approach is similarly reflected in the framework set out in the mandate documents, in that current and proposed regulation at national level also regulate these duties in commercial codes or civil codes. For example, the French Duty of Vigilance Law introduced two new articles (Articles L. 225-102-4 and L. 225-102-5) into the French Commercial Code. The Swiss counter-proposal seeks to introduce several articles in the Swiss Code of Obligations, the Swiss Civil Code and the Swiss Private International Law Act.

However, it should also be noted that the duty to be created would be a corporate duty for the company as a whole, rather than duties for individual directors. Where directors have fiduciary duties, they are usually only enforceable by the company or the shareholders, and not by external parties or stakeholders. The position is explained in the Netherlands country report as follows:[1061]

> It should be noted that even if a duty could be said to exist under certain circumstances for directors (or supervisory directors) of Dutch companies to take the interests of 'external' stakeholders in the IRBC-context into account, Dutch company law does not provide them with enforcement mechanisms to hold (officers of) the corporation liable for any damage suffered as a result of its operations. This also explains why there is no case law in the field of Dutch company law that specifically deals with irresponsible business conduct in global value chains. In

[1059] See Assessment of Options section below on the potential impacts on public authorities.
[1060] LeBaron and Rühmkorf, above n 830 at 15.
[1061] The Netherlands country report further adds: "One case that may be mentioned here is the 1979 Batco case, which involved inquiry proceedings into the affairs of the company Batco Nederland, following a dispute between the company and the labour unions over the company's decision to close one of its factories. The Enterprise Division of the Amsterdam Court of Appeal came to the conclusion that there had been mismanagement by Batco in this respect, since the company had contravened elementary principles of responsible entrepreneurship by failing to properly take into account the factory workers' interests. One of the court's considerations was that while the company had expressly accepted the OECD Guidelines for Multinational Enterprises as a guideline for its policies in these matters, it had failed to live up to its responsibility under those guidelines to consult with the unions and the works council."

theory, inquiry proceedings (the Dutch *enquêteprocedure*) could provide an option for 'external' intervention in order to address serious and ongoing violations of human rights or environmental standards that occur as part of the international business activities of Dutch companies (and/or their subsidiaries). These proceedings may also be instituted in the general interest by for example trade unions or the Advocate General at the Dutch Supreme Court. However, there are no examples to date of such proceedings being applied in the IRBC-context.

In any event, the creation of a corporate duty of due diligence would indirectly create fiduciary duties for the directors, who would need to ensure compliance with this duty in the interest of the company (but which duty is owed to the company i.e. the shareholders only). This legal duty would apply regardless of whether the individual director, company or shareholders apply an "enlightened" understanding of what is "material" or "in the company's interest". The same duty would apply to directors whether they believe sustainability issues to be in the company's long-term interest or not.

6. Due diligence as a legal standard of care: Clarification of a few common questions

During the course of the study, it became evident that it would be helpful to clarify[1062] a few common questions regarding due diligence as a legal standard of care (also referred to as a duty of care) within the context of human rights and environmental harms. This appeared particularly important in light of the limited number and relatively recent due diligence requirements of the nature considered in this study, as well as the various terminologies used in the legal systems set out in the country reports.

The following overview[1063] summarises the nature of due diligence as a legal standard or duty of care within the context of human rights and environmental harms. It is considered in more detail elsewhere in this study, including in the Country Reports, stakeholder views in Market Practices, and the discussion of Regulatory Options. This overview is guided by questions from or clarifications made by stakeholders and experts during the study.

Due diligence as a legal standard of care is based on the basic tort law or negligence principle - phrased differently but similar in nature across civil and common law jurisdictions - being that a person should take reasonable care not to cause harm to another person.[1064] This ties in with the description by John Ruggie, main author of the UN Guiding Principles on Business and Human Rights ("UNGPs"),[1065] of due diligence as a "do no harm" requirement.[1066] The OHCHR description of due diligence is helpful:[1067]

[1062] This is in accordance with EU Better Regulation Tool #17 Section V.

[1063] This section is included in the full report in the section Problem Analysis and Regulatory Options under the subheading "Due Diligence as a Legal Standard of Care: Clarification of a Few Common Questions".

[1064] See for example Cees van Dam, "Tort Law and Human Rights: Brothers in Arms: On the Role of Tort Law in the Area of Business and Human Rights" (2011) 2 *JETL* 221.

[1065] UN Office of the High Commissioner for Human Rights "Guiding Principles on Business and Human Rights: Implementing the "Protect, Respect and Remedy' Framework", HR/PUB/11/04, 2011, available at: https://www.ohchr.org/documents/publications/GuidingprinciplesBusinesshr_eN.pdf.

[1066] Ruggie summarises the corporate responsibility to respect as "put simply, to do no harm". UN Human Rights Council, "Report of the Special Representative of the Secretary-General on the issue of human rights and transnational corporations and other business enterprises: 'Protect, Respect and Remedy: a Framework for Business and Human Rights'", A/HRC/8/5 (7 April 2008), at para 24; UN Human Rights Council, "Report of the Special Representative of the Secretary-General on the issue of human rights and transnational corporations and other business enterprises: Clarifying the Concepts of 'Sphere of Influence and Complicity'", A/HRC/8/16 (15 May 2008), at para 3.

[1067] Office of the UN High Commissioner for Human Rights, *The Corporate Responsibility to Respect Human Rights: An Interpretive Guide* (2012) at 4.

> Such a measure of prudence, activity, or assiduity, as is properly to be expected from, and ordinarily exercised by, a reasonable and prudent [person or enterprise] under the particular circumstances; not measured by any absolute standard, but depending on the relative facts of the special case. In the context of the Guiding Principles, human rights due diligence comprises an ongoing management process that a reasonable and prudent enterprise needs to undertake, in light of its circumstances (including sector, operating context, size and similar factors) to meet its responsibility to respect human rights.

As a legal standard of care, the level of due diligence expected therefore depends on the relevant circumstances in which the company operates, and is both a process and an approach. Due diligence looks at how the company identifies, assesses and addresses human and environmental impacts of the company's activities.

Due diligence in our context is generally considered to be a continuous and ongoing process comprised of four stages:[1068]

1. Identification and assessment of actual and potential impacts that company may cause or contribute to through its own activities, or which may be directly linked to its operations, products or services by its business relationships;
2. Acting upon the findings of that assessment and integrating its findings about its impacts into decision making;
3. Tracking the company's efforts to address its impacts, to ensure they these actions effective
4. Communicating how the company is addressing its impacts.

These stages are circular in that they operate as part of a continuous process.

The first steps which a company is expected to take are based on identification and risk assessment. This starts with identifying and assessing the risk of harm to those affected by the company and then the consequent risk to the company. It does not commence with the risk to the company. To identify the risk of harm requires a full risk assessment.

Once that full assessment has occurred and is reviewed at senior level, the company can create and act on its policies in this area. It can also then determine its priorities in dealing with the risk as part of its due diligence process. Those priorities must not be set in advance, or some serious risks will be missed, and these risks will vary from company to company, and over time. The focus is on dealing with serious or salient risks first. Salient issues are those that are at risk of the most severe negative impacts through a company's activities or business relationships. The salient issues can best be discerned after the assessment of the company's impacts undertaken, so that material risks are not predetermined.

Due diligence then requires a company to ensure that it tracks its actions and policies in response to this risk assessment. This must be right to the operational level and into its supply and value chain. It needs to report back on this tracking and then communicate both internally and externally about it.

These risks will depend from one company to the next. Due diligence is useful for the regulation of corporate conduct, as it does not require the regulator to attempt to do the company's impact assessments for them. Regulators cannot realistically list every single circumstance, or combination of circumstances, which could possibly apply to companies on

[1068] As defined in the Terms of Reference ("TOR"), mandate materials and UNGP 17.

a daily basis in different parts of their global operations. Instead, regulators use due diligence as a legal standard of care to expect the company to assess its own risks and address them in accordance with the standard of care. If the company exercises reasonable or adequate due diligence, it meets the standard. If it does not, for example because it overlooked certain risks factors which it should have taken into account, then it does not meet the standard.

With due diligence as a legal standard of care, the regulator sends the message that society requires companies to take full responsibility for their own harmful impacts, and that failure to do so attracts legal liability.

In some instances, the company operates in a high risk sector or country. If so, the company must take these additional risk factors into account, including the legal and social environment. Due diligence expressly does not automatically expect companies operating in high risk contexts to leave, and does not intend to penalise those companies which operate in certain countries or sectors. Indeed, it has been well-demonstrated that there are no countries or sectors which pose no risks at all to people, the environment or the planet.

Due diligence expects companies to assess for themselves their risks, prevent such risks from taking place, and mitigate any damages which have already occurred. The occurrence of a harm suggest that the company would be liable, unless it could show that it has done everything that could have been reasonable expected in the circumstances. In this way, the due diligence standard incentivises effective, high quality and practical due diligence processes which target real risks and priorities.

There is a distinction between due diligence as a legal standard or duty of care and due diligence as a procedural requirement. Where the first sets out the general duty of "do no harm", the second could be viewed as adding a procedural requirement of taking proactive and demonstrable steps. For example, the proposal for mandatory due diligence in Switzerland and the draft law in Germany are understood to require due diligence as a legal standard or duty of care, whereas the French Duty of Vigilance Law has an additional component of publishing a vigilance plan. It is not clear that in terms of liability anything would turn on this distinction, as in both cases the breach of the duty would be triggered if the due diligence requirement was not met and a damage resulted (or could result) from the breach.

In addition, both these forms of *mandatory due diligence* (as a legal standard of care, or requirement) can be distinguished from a *duty to prevent* certain harms (such as set out in the UK Bribery Act). A duty to exercise due diligence is breached when the company *fails to exercise the required standard of due diligence* (or where the company fails to put in place a due diligence process, if there is a procedural requirement). In contrast, the duty to prevent is breached if the company *fails to prevent the harm*. As demonstrated by the UK examples of duty to prevent laws (for failing to prevent bribery[1069] and failing to prevent tax evasion[1070] respectively), these laws create strict (or "no fault") liability, and would ordinarily need to accompanied by a statutory defence of due diligence, so as to ensure that they do not create an absolute liability with no defence.

With both mandatory due diligence and the duty to prevent model, there is the ability for claimants to take preventative legal action for harms which have not yet occurred. Where the duty is framed with reference to due diligence for *actual or potential* harms, it would be possible for claimants to bring a preventative claim on the basis that the company is failing to meet the standard of due diligence required for actual or potential harms. Preventative

[1069] Section 7 of the UK Bribery Act 2010.
[1070] Sections 45(2) and 46(3) of the UK Criminal Finances Act 2017.

relief may include injunctive relief such as a court ordering the company to improve its due diligence and pay interim damages. An example of a law which provides for this preventative relief for potential future harms is the French Duty of Vigilance Law. Similarly, any state-based oversight body could investigate and sanction a failure to meet the standard regardless of whether a harm already took place, or may occur unless the process is improved.

In addition, with a mandatory due diligence duty which is overseen and enforced by the state or independent oversight body, the regulator could also review and take action against a company's process even where no claimant has alleged an actual or potential harm. This review would still evaluate the adequacy or appropriateness of the company's due diligence steps with reference to the context and the possible harm which *could* arise from the company's failure to exercise its duty of care, but the oversight could be triggered by the regulator itself, even in the absence of any claimants.

Another key feature of due diligence as a standard of care as highlighted by stakeholders and experts is that it should not be construed as a "tick-box" exercise. For example, the EU Timber Regulation[1071] and the EU Conflict Minerals Regulation[1072] both recognise that certain third party verification schemes could be used as part of the risk assessment process. However, these verifications are not described as replacing the due diligence requirements, which place the risk assessment duty on each individual company ("operator") regardless of whether they have acquired formal certification. For instance, the Commission Implementing Regulation on the Timber Regulation specifies that certain certification or other third-party verified schemes *may* be taken into account in the risk assessment and risk mitigation procedures,[1073] but does not provide that such verification tools can be used "on [their] own to evidence compliance with the Timber Regulation".[1074]

[1071] Recital 19 of the EU Timber Regulation, EU Regulation No 995/2010 of the European Parliament and of the Council laying down the obligations of operators who place timber and timber products on the market, provides: "In order to recognise good practice in the forestry sector, certification or other third party verified schemes that include verification of compliance with applicable legislation *may* be used in the risk assessment procedure." [Our emphasis]. See also Articles 4 and 6, including 6(1)(b) which requires: "(b) risk assessment procedures *enabling the operator to analyse and evaluate the risk* of illegally harvested timber or timber products derived from such timber being placed on the market. Such procedures shall take into account the information set out in point (a) as well as relevant risk assessment criteria, *including*: - assurance of compliance with applicable legislation, which *may include certification or other third-party- verified schemes* which cover compliance with applicable legislation, - prevalence of illegal harvesting of specific tree species, - prevalence of illegal harvesting or practices in the country of harvest and/or sub-national region where the timber was harvested, including consideration of the prevalence of armed conflict, - sanctions imposed by the UN Security Council or the Council of the European Union on timber imports or exports, - complexity of the supply chain of timber and timber products." [Our emphasis]

[1072] Recital 14 of the EU Conflict Minerals Regulation, EU Proposal for a Regulation of the European Parliament and of the Council setting up a Union system for supply chain due diligence self-certification of responsible importers of tin, tantalum and tungsten, their ores, and gold originating in conflict-affected and high-risk areas, COM/2014/0111 final - 2014/0059 (COD), provides: "Union importers retain individual responsibility to comply with the due diligence obligations set out in this Regulation. However, many existing and future supply chain due diligence schemes ('due diligence schemes') *could contribute* to achieving the aims of this Regulation…Such schemes use *independent third-party audits to certify smelters and refiners that have systems in place to ensure the responsible sourcing of minerals.* It should be possible to recognise those schemes in the Union system for supply chain due diligence ('Union system'). The methodology and criteria for such schemes to be recognised as equivalent to the requirements of this Regulation should be established in a delegated act to allow for compliance with this Regulation by individual economic operators that are members of those schemes and to avoid double auditing. Such schemes should incorporate the overarching due diligence principles, ensure that requirements are aligned to the specific recommendations of the OECD Due Diligence Guidance and meet the procedural requirements such as stakeholders' engagement, grievance mechanisms and responsiveness." [Our emphasis]

[1073] Article 4 of the EU Commission Implementing Regulation No 607/2012 of 6 July 2012 on the detailed rules concerning the due diligence system and the frequency and nature of the checks on monitoring organisations as provided for in Regulation (EU) No 995/2010 of the European Parliament and of the Council laying down the obligations of operators who place timber and timber products on the market.

[1074] ClientEarth and Global Witness, "Strengthening Corporate Responsibility: The case for mandatory due diligence in the EU to protect people and the planet", 8 August 2019, available at: https://www.documents.clientearth.org/wp-content/uploads/library/2019-07-23-strenghtening-corporate-responsibility-the-case-for-mandatory-diligence-in-the-eu-to-protect-people-and-the-planet-coll-en.pdf at 14.

In other words, the legislation does not itself provide for such certifications to operate as "exempting"[1075] companies from their due diligence duties.

These provisions of the EU Timber Regulation were interpreted and applied in the German Administrative Court in Cologne. The Court found against a German company which sourced timber from a supplier in DRC, on the basis that the company should have recognised that the certificate produced by the supplier was fake. As the defendant company failed to recognise this, they were found not to have met the due diligence requirement, which the Court emphasised is "not merely a purely formal requirement".[1076] The Court also referred to the seriousness of these requirements in light of the role which illegal logging plays in climate change.[1077]

In this way, the provisions of the EU Timber Regulation which require due diligence (or in this case risk assessment) extends wider than a mere "tick-box" of formalities, to a realistic consideration of all the risk factors applicable in the circumstances.

This understanding of due diligence aligns with other examples of how due diligence as a legal standard of care is applied in the case law. Such due diligence enquiries typically ask not only about the formalities of the process but whether it was adequate in the circumstances, and whether it was followed in reality. The simple fact of having a so-called "due diligence" process in place does not automatically show that the standard of care was met. For example, in the case of *Eric Barizaa Dooh of Goi and others v Royal Dutch Shell*, the Court of Appeal of The Hague described the following factual enquiry of not only the process but its adequacy and implementation in the circumstances:[1078]

> The assertion by Shell that the parent company did *not know* about the spillage and the condition and maintenance of the pipeline locally does not seem to be an adequate defence in all cases, particularly not if sabotage ceases to be a cause of damage. Considering, *inter alia*, (i) that Shell sets itself goals and ambitions with regard to, for instance, the environment, and has defined a group policy to achieve these goals and ambitions in a coordinated and uniform way, and (ii) that RDS (like the former parent company) monitors compliance with these group standards and this group policy, such questions arise as: (a) which (maintenance) standards applied to an old pipeline whose insides were no longer monitored like the one in question; (b) were these maintenance standards complied with; (c) if so, what is this evidenced by, and if not, shouldn't this have been noted within the context of the supervision performed by the parent company (the audits); (d) shouldn't it have been noted with an adequate reporting system in place and (e) why was it not. Another question is (f) whether the parent company -considering the autonomy and individual responsibility of (the management of) SPDC- was sufficiently equipped (as

[1075] For example, see Cara-Sophie Scherf, Peter Gailhofer, Nele Kampffmeyer, Tobias Schleicher "Responsibility towards society and the environment: businesses and their due diligence obligations Background paper from the research project commissioned by the Federal Environment Agency", August 2019, German Federal Ministry for the Environment, Nature Conservation and Nuclear Safety, available at: https://www.umweltbundesamt.de/publikationen/umweltbezogene-menschenrechtliche at 7.

[1076] At para 49: "Bei dieser Verpflichtung handelt es sich nicht nur um eine rein formale Anforderung, sondern die Dokumente oder anderen Nachweise müssen inhaltlich zutreffend und verlässlich sein. Allein die Vorlage des - wie darzulegen sein wird - gefälschten Teil-Zertifikats vom 29. Dezember 2012 für die hier in Rede stehenden 16 Stämme Wengé-Holz genügt dieser Pflicht nicht. Bei einer anderen Sichtweise liefe der Zweck der Norm leer." The Court also found at para 61 that the fact that the countries like the DRC have well-known corruption risks is unfortunate for the importing company, but that this does not diminish the due diligence requirements.

[1077] At para 66.

[1078] *Eric Barizaa Dooh of Goi and others v. Royal Dutch Shell Plc and Others*, Court of Appeal of the Hague, 200.126.843 (case c) + 200.126.848 (case d), December 18, 2015, at para 6.9. On this case, see for instance Claure Bright, "The Civil Liability of the Parent Company for the Acts or Omissions of Its Subsidiary: The Example of the *Shell* Cases in the UK and in the Netherlands", in Angelica Bonfanti (ed.) *Business and Human Rights in Europe: International Law Challenges* (2018) 212 at 220.

far as knowledge, possibilities and means are concerned) to intervene adequately in case of evident negligence by SPDC.

Similarly, in other cases where due diligence is required, the courts consider whether there was a process in place, whether the process was implemented, and whether it was adequate. In English case law relating to statutory due diligence defences, courts and regulatory bodies have considered management's telephonic availability,[1079] whether incidents were recorded in logbooks,[1080] whether advice from external experts were sought,[1081] whether training programmes effectively imparted sufficient knowledge and understanding to prevent the incident from taking place,[1082] as well as the expertise of the trainers.[1083] It has also been held that having an audit system in itself does not constitute adequate due diligence as it was not constructed to "pick up [the] failure" and did not in fact prevent or address the impacts in question.[1084]

Some laws expressly provide for a due diligence defence, such as the Swiss legislative proposal and the UK Bribery Act. However, as long as the legal duty does not envision absolute liability, it is always available for a party to argue, in its defence, that it has met the standard required by the duty, or in other words, to deny that it has breached the duty of due diligence. Stakeholders have also pointed out that in accordance with many existing laws, companies are not provided with a defence of having performed due diligence. Examples include environmental laws which create offences for companies which have caused damage, as well as other areas of criminal law relating to tax and health and safety. Stakeholders emphasised that in these cases a due diligence standard should not "water down" these existing offences by providing for a due diligence defence where there currently is none.

Another key feature of due diligence under consideration in this study is its focus on risks that go beyond the company's risks to those external risks which affect people the environment and the planet. As described elsewhere in this study, the OECD Guidelines have expanded the UNGPs concept of human rights due diligence also to apply due diligence to risks related to conflict, human rights, labour rights, environment, bribery and corruption, disclosure and consumer interests.[1085] The non-binding guidance to the EU Non-Financial Reporting Directive also discusses an expanded concept relating to risks external to the company.[1086] Stakeholders have indicated that this signifies a significant shift in corporate risk management, which is necessitated by the due diligence standard. Although it takes time to implement this shift into real practices, this trend seems to be irreversible,

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[1079] See *R. (on the application of Tesco Stores Ltd) v City of London Corp* [2010] EWHC 2920 (Admin) paras 10 and 26. In this case, the due diligence defence set out in the section 21 of the then UK Food Safety Act 1990 read with Regulation of the Food Hygiene (England) Regulations 2006 was applied. See also *Lincolnshire County Council v Safeway Stores Plc* (1999) EHLR Dig 456 where the defendants successfully relied on the defence of due diligence on the basis of having an adequate system in place. See also Robert McCorquodale, Lise Smit, Stuart Neely and Robin Brooks, "Human Rights Due Diligence in Law and Practice: Good Practices and Challenges of Business Enterprises" (2017) 2 *Business and Human Rights Journal* 195–224.

[1080] *London Borough of Croydon v Pinch A Pound UK Ltd* [2010] EWHC 3283 (Admin) at 34; *Tesco v London,* ibid, at paras 15 and 22-23.

[1081] *Croydon*, ibid, at para 30.

[1082] For example, see *Tesco v London,* above n 1079 at paras 9 and 11; *Croydon,* ibid at para 29.

[1083] *Croydon,* ibid, at paras 30 and 33.

[1084] *Tesco v London,* above n 1079 at para 26.

[1085] Organisation for Econom
ic Cooperation and Development (OECD), Guidelines for Multinational Enterprises, 2011 ("OECD Guidelines").

[1086] For example, the EU Non-Binding Guidelines on non-financial reporting (methodology for reporting non-financial information) (2017/C 215/01) of June 2017, state at 3.1: "Companies are expected to consider the actual and potential severity and frequency of impacts. This includes impacts of their products, services, and their business relationships (including supply chain aspects)." Moreover, the EU Non-Binding Guidelines on Reporting Climate-Related Information state at 2.3: "Unless otherwise stated in the text, references to risks should be understood to refer both to risks of negative impacts on the company (transition risks and physical risks – see below) and to risks of *negative impacts on the climate*. …Both of these kinds of risk – risks of negative impacts on the company and risks of negative impacts on the climate – may arise from the companies own operations and may occur *throughout the value chain*, both upstream in the supply-chain and downstream." [Our emphasis] particularly with the recent statement by the Business Roundtable that the purpose of the corporation extends to the interests of stakeholders.[1087]

Lastly, a core feature of due diligence is its focus on the steps which are expected of the individual company: a company can only be held legally liable for not identifying, assessing, prevent and mitigating its own impacts, or the impacts which it could be reasonably expected to control or influence through its business relationships. Stakeholders in the study have noted that in this way, a due diligence standard should not operate to hold companies liable for systemic issues, which cannot be remedied by a single company, if the company has done all it can do prevent harms resulting from its own operations.

6.1 Distinction from legal compliance with existing laws

As due diligence is a "do no harm" requirement, the due diligence under discussion in this study should be distinguished from the ordinary understanding of due diligence for compliance with laws. Due diligence in this context relates to due diligence for *harms*, rather than due diligence for *legal compliance*.

The existing and proposed laws which require companies to exercise due diligence discussed in this study all focus on the steps which the company takes to prevent certain harms (deforestation, child labour, modern slavery). Yet these laws do not simply prohibit the unwanted outcomes, through absolute liability without a defence (for example, the model used in many environment and health and safety laws). Instead, the duty is concerned with whether the company has exercised due diligence to prevent or address these harms. The due diligence duty therefore has two components: the actual or potential harm, as well as the company's steps in relation to those.

Due diligence requires companies to take steps to address relevant harms *regardless* of whether they are permitted or prohibited by the laws of the countries where they take place. In many cases, these harms would in any event be illegal under the laws of the host state where they take place and / or the home state of the company (such as slavery or forced labour), but in other cases they may be perfectly legal, or even required by, national law (such as where the relevant national law does not require free, prior and informed consent, or where local laws are discriminatory against LGBTI persons).

Accordingly, due diligence in this study does not concern due diligence for compliance with existing laws, which companies are already required to comply with. Due diligence a legal standard of care would be an additional legal duty, which does not currently exist in this context. The UNGPs describe this as follows:[1088]

> The responsibility to respect human rights is a global standard of expected conduct for all business enterprises wherever they operate. It exists independently of States' abilities and/or willingness to fulfil their own human rights obligations, and does not diminish those obligations. And it *exists over and above compliance with national laws and regulations* protecting human rights. [Our emphasis]

Similarly, Bonnitcha and McCorquodale[1089] highlight that due diligence in this context should be distinguished from the commonly used term of "due diligence" in day-to-day business language, which refers to a once-off, but not usually legally required, review of legal compliance and other risks before a transaction, merger or investment takes place.

[1087] US Business Roundtable, "Statement on the Purpose of a Corporation", August 2019, available at: https://opportunity.businessroundtable.org/wp-content/uploads/2019/08/Business-Roundtable-Statement-on-the-Purpose-of-a-Corporation-with-Signatures.pdf.
[1088] Commentary to UNGP 11.
[1089] Jonathan Bonnitcha and Robert McCorquodale, "The Concept of 'Due Diligence' in the UN Guiding Principles on Business and Human Rights", 28 *European Journal of International Law* (2017) 899 at 900.

6.2 Distinction from other models of regulation

In light of the above, it is important to distinguish due diligence as a legal standard of care from other models of regulation.

Due diligence is not itself a reporting requirement, nor is it a disclosure requirement. It is also not a "list" of activities which a company needs to undertake, nor a list of issues which a company needs to consider.

Although due diligence as described in the UNGPs has a component of "communication", this does not exclusively refer to public reporting in corporate reports, but also includes wider public engagement and consultation with stakeholders. It is noted also that due diligence reporting requires publication of information relating to the due diligence, i.e. the *steps or actions taken* or put in place, including on the effectiveness of these measures, and not necessarily of the actual adverse impacts identified, which in many cases may contain sensitive information. Therefore, reporting or disclosure may or may not be undertaken as part of meeting the standard of due diligence. In some cases, as with certain SMEs, disclosure may not be required or reasonable, as long as the standard of care is met.

Recent reporting requirements such as those under consideration in this study ask companies to report on their due diligence steps. Although these laws do not establish a legal duty to undertake due diligence, the terminology of due diligence as used by reporting requirements may have contributed to a perception that due diligence is the same as reporting.

This, in turn, may have contributed to the impression amongst stakeholders, evidenced in the Market Practices section, that due diligence would require an administrative burden or compliance exercise which would be disproportionate for SMEs with less resources to undertake. In many instances due diligence can operate as part of existing processes, such as on health and safety, and with labour relations.

However, due diligence standards, including the UNGPs and OECD Guidelines, describe the appropriate due diligence measures taken to be proportionate to risk, and expressly refer to the limited resources of SMEs in this regard. Shift has also highlighted[1090] what some of stakeholders have pointed out: that SMEs may need to take significantly less due diligence steps than their larger peers, insofar as smaller companies have smaller footprints, fewer employees, and their internal risk management processes are often within the knowledge control of one or a few individuals. In this way, economies of scale do not necessarily apply to due diligence: a larger company with a larger footprint is likely to require significantly more formal, structured and sophisticated processes than a local micro business.

6.3 Interaction with existing laws and other regulatory options

Due diligence as a legal standard differs from the requirements of the EU Non-Financial Reporting Directive, and other corporate reporting requirements which, even when they take a wider view of the external sustainability risks on in the long term, nevertheless require information relating to material or principal risks to the company's performance.

For example, the Non-Binding Guidelines on Reporting Climate-Related Information in terms of the EU Non-Financial Reporting Directive describe the "double materiality perspective" which focuses not only on "financial materiality", but also on the impacts of its

[1090] Francis West for Shift, "SMEs and the Corporate Responsibility to Respect Human Rights
Busting the Myth that Bigger is Always Better" May 2019, available at:
https://www.shiftproject.org/resources/viewpoints/busting-myth-smes-corporate-responsibility-respect-human-rights/.

activities, described as "environmental and social materiality".[1091] Whereas the former is focused on the interests of investors, the latter is "typically of most interest to citizens, consumers, employees, business partners, communities and civil society organisations".[1092] However, as is evidenced by the Country Reports, this new understanding of the double materiality perspective is yet to be applied by regulators within Member States in overseeing compliance with the relevant national laws on corporate reporting which implement the Directive.[1093] Instead, Member States' implementation have taken place in the context of corporate reporting laws which have traditionally focused on the materiality of the impacts of the company's activity on the company's (short or long term) performance. Furthermore, despite described in the Non-Binding Guidance as having an interest in the "environmental and social materiality", the Directive does not provide external stakeholders with a right of action in case of a failure to report on such information.

In contrasting due diligence with the requirements of corporate reporting, the question as to whether an external harm will, in the long or short run, affect the company's performance is *irrelevant* for the purposes of due diligence as a legal standard. Due diligence as a legal standard or duty of care requires companies to exercise the care required to prevent and address external harms, *regardless* of whether these are harms beneficial, detrimental or neutral to the company's performance in the long or short run.

Reporting standards require companies to report on the steps they have taken, but do not legally require them to take any steps towards meeting a certain standard of care. So a reporting requirement could be satisfied by referring in a public report to specific processes which would not constitute adequate due diligence. The reporting requirements under discussion in this study do not have a built-in test of the adequacy of the steps or processes which are reported. Where reporting requirements are enforced, either by shareholders or regulators, this usually relates to matters such as whether there was a report which contains the required information, the veracity of the information reported, and whether any materials risks were omitted.

Many existing corporate reporting requirements, including the EU Non-Financial Reporting Directive, require reporting on aspects which would be included as part of a due diligence obligation. The EU Non-Financial Reporting Directive is fairly new, and similar reporting requirements in other areas of corporate law, such as section 172 of the UK Companies Act, are yet to be enforced by regulators (see UK country report). Insofar as reporting requirements are centred around those risks that are material to the company, a mandatory due diligence duty would serve to clarify what constitutes material information. If there is a law requiring a standard of care which could lead to legal liability, it is unlikely that a director could argue that any risks relating to this duty would not constitute material information.

Reporting and due diligence requirements are therefore complementary, and potentially interact with one another. For example, as evidenced in various cases, and described by interviewees, publicly reporting on steps taken should help a company prove that it has undertaken due diligence. Reporting on due diligence steps taken would therefore be in the company's interest once a duty to undertake due diligence is established, although the due diligence standard would not in itself proscribe the extent or detail reporting required. Instead, reporting would be part of the company's risk management in terms of its due

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[1091] Non-binding guidelines on reporting climate-related information above n 1086 at 2.2.

[1092] Ibid.

[1093] Neither the EU Non-Financial Reporting Directive itself, nor the June 2017 Non-Binding Guidance refers to "double materiality" or to "financial materiality" or "environmental and social materiality". These concepts were introduced by the Non-Binding Guidance on Reporting Climate-Related Information during the course of this study, in June 2019. The Directive refers to the "impacts of [the company's] activity" in Art 19a(1).

diligence. As far as a due diligence duty of care is concerned, certain sensitive findings may be omitted from company reporting, as long as it is reasonably or adequately addressing these impacts on an ongoing basis and proportionately to the severity of the risk.

In turn, a mandatory due diligence duty would influence and complement existing reporting requirements, which ask companies to report on the steps they have undertaken. (The due diligence which they undertake in terms of the mandatory due diligence duty would of course also be included in these steps.) A duty of care of due diligence would provide focus and confirmation of what kind of information is material or expected in terms of specific reporting requirements. This would provide significant clarity where currently the concept of "materiality" still seems to be unclear, and, as noted by stakeholders in this study, often dependent on individual directors and shareholders' persuasions regarding the "business case" benefits of voluntary sustainability for the company.

For those companies that are already undertaking those due diligence steps in order to report on them, a due diligence duty would not necessarily constitute a significant additional burden. For those companies that are simply reporting without having any substantive due diligence on which to report, a due diligence duty would require an evaluation of whether they are undertaking adequate risk management steps, for the purposes of both the due diligence duty and the reporting requirement.

In addition, the due diligence standard would also influence the fiduciary duties of directors. Although the due diligence duty would apply to the company, the company would be liable in the case of failing to meeting the standard, which in turn would influence the fiduciary duty of the directors, namely to act in the interest of the company. In this way, the due diligence duty would inform how and to what extent directors are expected to undertake risk management for these external harms. Without this legal duty, some of these external harms may not otherwise be viewed as posing materials risks for the company's performance.

In addition to existing reporting requirements, there are multiples of other existing laws that apply, both at EU and Member State level, to corporate activities and their impacts on people, the environment and the planet. These laws already have the intention, and effect, of preventing such harms by business, especially with regard to their own activities within the EU itself. These laws would likely influence the content of the standard which is expected under each individual circumstance. If companies are complying and satisfied that they are preventing their harms in accordance with these laws, they may also be able to demonstrate that they are thereby meeting their due diligence standard, unless there are additional or severe impacts at stake in the specific circumstances.

6.4 Non-binding guidance

As noted above, due diligence is not a list of requirements that companies need to "tick off". Regardless of how detailed such a list would be, all the possible risk factors would never all be applicable to the same company. If companies were required to "tick off" such lists regardless of whether these risks even apply to the particular company in question, the law would possibly operate in a prohibitively burdensome way. The OHCHR has warned against the risks of a duty that "overly detailed and proscriptive" as this may lead to "narrow, compliance-orientated, 'check-box'" processes.[1094]

However, the concept of due diligence is by its nature wide, and it often takes several years for courts and industries to flesh out the content of how such standards would be applied.

[1094] OHCHR, "Improving accountability and access to remedy for victims of business-related human rights abuse: the relevance of human rights due diligence to determinations of corporate liability", UN Doc. A/HRC/38/20/Add.2, 1 June 2018 at 17 and 18.

For this reason, regulators at national level have made use of guidance to inform the implementation of due diligence standards in other areas. Such non-binding but influential guidance would ordinarily provide examples of some of the factors that companies could take into account, without requiring them to "tick off" steps that are not applicable to their risks. It informs all parties of how the law is likely to be applied, including companies that have to put in place procedures, claimants who seek to ascertain whether they may have a cause of action, and regulators and courts who are mandate with applying the law. In this way, non-binding guidance is commonly used to perform immediately the function which case law and evolving practice would otherwise take years to achieve.

In the absence of dedicated non-binding guidance accompanying a specific due diligence measure, existing guidance, laws and standards could nevertheless inform the development and application of a due diligence standard. However, without the influential authority of dedicated non-binding guidance, companies may have less legal certainty about the application and relevance of these standards.

It is noted that where examples of risk factors are listed in non-binding guidance, each factor will still just be one aspect which the company would be expected to take into account. For example, a company is not seen as failing in its due diligence expectations simply because it operates in a high risk environment. Instead, the question is how the company addresses these risks. What is the size and nature of the company and how does it identify, prioritise and prevent or mitigate its risks? Does it have leverage, and if so, how is it exercising it? How is it increasing its leverage?[1095] Only if the company has no leverage, and any attempts at increasing leverage are unsuccessful, would a company be expected to consider leaving a jurisdiction, although this may be the necessary outcome. This may differ dramatically from one company to the next, even within the same "high risk" country or "high risk" sector, depending on the steps which the company is taking to identify, assess, prevent and mitigate any actual or potential harms.

Through undertaking due diligence, companies are expected to understand and assess their risks and put in place real and effective processes to manage their risks. Often, those companies that have high risks, and have as a result faced public allegations, are the ones are taking action to improve their risk management actions.[1096] These companies may score very low on any "tick-box" list by virtue of the countries or contexts where they operate. However, if the quality of their real processes are considered and evaluated, they may likely be deemed to meet the standard better than a company which operates in what it perceives as a low risk context and has therefore never assessed its external risks.

Finally, undertaking due diligence can have positive impacts for a company. As the OECD Guidance on Due Diligence for Responsible Business Conduct makes clear:[1097]

> Effectively preventing and mitigating adverse impacts may in turn also help an enterprise maximise positive contributions to society, improve stakeholder relationships and protect its reputation. Due diligence can help enterprises create more value, including by: identifying opportunities to reduce costs; improving understanding of markets and strategic sources of supply; strengthening management of company-specific business and operational risks; decreasing the probability of incidents relating to matters covered by the OECD Guidelines for MNEs; and decreasing exposure to systemic risks. An enterprise can also carry out due diligence to help it meet legal requirements pertaining to specific [Responsible Business Conduct] issues, such as local labour, environmental, corporate governance, criminal or anti-bribery laws.

[1095] Commentary to UNGP 19.
[1096] See for example McCorquodale et al above n 1079.
[1097] OECD "OECD Guidelines for Multinational Enterprises: Responsible Business Conduct Matters", available at: http://mneguidelines.oecd.org/MNEguidelines_RBCmatters.pdf at 16.

In this way, it is clear that due diligence as a legal of standard of care operates as a risk management exercise for the company. The more accurate and engaged the due diligence, the higher the likelihood that the company will be able to identify, prioritise and address its most severe risks in reality.

7. Further considerations around scope of application

A few further considerations are relevant to the discussion of regulatory options for intervention. These were not discussed above as separate sub-options, as they relate to questions that apply to all of the above options.

7.1 Accompanying non-binding guidance on the mandatory duty

As evidenced in the Market Practices section, several stakeholders emphasised that in order to create a "level playing field", there is a need for a wide and general legal duty, but it was also emphasised across the spectrum that, similar to due diligence in the UNGPs and the OECD Guidelines, the content of the duty would need to be informed by the circumstances of each context.

This balance was also described by the UN OHCHR in its 2018 report on domestic laws requiring due diligence as a standard of conduct assorted with a legal liability regime:[1098]

> Such laws can give companies clarity with respect to the human rights due diligence activities they are required to perform. This could help create a level playing field for companies, give human rights due diligence clear legal force, educate stakeholders and the wider public about company activities, and ultimately reduce risks of adverse human rights impacts from occurring.

However, the report also warns against the unintended consequences that can result from having overly detailed due diligence regulation:[1099]

> The possibility that *overly detailed and proscriptive* legal regimes could discourage innovation and proactive behavior by companies and encourage *narrow, compliance-orientated, "check-box"* human rights due diligence processes…On the other hand, too much flexibility may not provide sufficient levels of legal certainty for companies (especially if criminal sanctions are to be applied) and could make the regime difficult to enforce.
>
> This balance can be difficult to strike in practice, and States should give careful thought to the policy aims of legislation when reconciling these competing considerations. [Our emphasis]

The challenge of striking this balance between a general duty and specific certainty about its potential application in different circumstances was addressed in the case of the EU Non-Financial Reporting Directive with accompanying non-binding guidance. Article 2 of the directive provides in particular that:

> [T]he Commission shall prepare non-binding guidelines on methodology for reporting non-financial information, including non-financial key performance indicators, general and sectoral, with a view to facilitating relevant, useful and comparable disclosure of non-financial information by undertakings. In doing so, the Commission shall consult relevant stakeholders.

[1098] UN Human Rights Council, above n850 at para 16.
[1099] Ibid at paras 17 and 18.

Recital 17 of the Directive specifies that in preparing these non-binding guidelines "the Commission should take into account current best practices, international developments and the results of related Union initiatives".

As a result, the Commission has published non-binding guidelines on the methodology for reporting non-financial information in 2017,[1100] and guidelines on reporting climate-related information in 2019,[1101] to accompany the EU non-financial reporting Directive. These guidelines were adopted after the NFRD and it is possible that further guidance may be added, as the needs and context develop.

Although the guidelines are expressly non-binding, they have been influential in understanding the application and implementation of the measure.

It was noted by various stakeholders in our Market Practices section that an EU-level legislation requiring mandatory due diligence could be similarly complemented by non-binding guidance in order to inform the implementation of the measure over time. This would allow for the regulation envisaged not to be too prescriptive and for its content to apply widely. It would also allow for the due diligence standard to adapt to specific sectors, contexts, issues and types of companies, which differs widely in practice.

For instance, a report of the UN Working Group on the issue of human rights and transnational corporations and other business enterprises highlighted that:[1102]

> [T]he development of specific guidance for different types of businesses (e.g., informal businesses, small and medium-sized enterprises and multinational corporations) would be useful. Similarly, business enterprises operating in different sectors might benefit from supplementary guidance tailored to the specific challenges they face.

In this way, the benefits relating to influence and low implementation costs discussed in Option 2 of the Regulatory Options in this study could be harnessed, but with the additional benefits of the accompanying binding duty, which has been indicated to be the biggest weakness of voluntary guidance.

Non-binding guidance accompanying a general due diligence regulation could include some the following. Note that this is not an exhaustive list, but a selection of some standards and guidance which were named by stakeholders during the course of this study:[1103]

Reference to international standards such as:

- The UN Guiding Principles on Business and Human Rights
- The OECD Guidelines

[1100] Communication from the Commission, "Guidelines on non-financial reporting methodology for reporting non-financial information", 2017/C 215/01, available at: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52017XC0705(01).
[1101] Communication from the Commission, "Guidelines on non-financial reporting: Supplement on reporting climate-related information", 2019/C/01, available at: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52019XC0620(01).
[1102] Report of the UN Working Group on the issue of human rights and transnational corporations and other business enterprises, "Gender dimensions of the Guiding Principles on Business and Human Rights", A/HRC/41/43 (23 May 2019) at para 10.

[1103] Please note that this list provides only some examples which were listed by stakeholders. In this area there are a wealth of tools and guidance and it would fall outside the scope of this study to compile a comprehensive list. Please also see the Business and Human Rights Resource Centre which provides a detailed resource of materials, tools, and guidance, available at: www.business-humanrights.org.

- The OECD Due Diligence Guidance for Responsible Business Conduct: which provides practical support to companies on the implementation of the due diligence requirements contained in the OECD Guidelines.

Reference to existing sector-specific guidance and initiatives such as:

- The OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas
- The OECD Due Diligence Guidance for Meaningful Stakeholder Engagement in the Extractive Sector
- The OECD Due Diligence Guidance for Responsible Supply Chains in the Garment and Footwear Sector
- The OECD-FAO Guidance for Responsible Agricultural Supply Chains
- The Better buying Initiative:[1104] which is a unique system for suppliers to communicate with their buyers about purchasing practices.

Reference to sector-specific industry programmes such as:

- The industry schemes set up to support responsible minerals sourcing such as, for instance:
    - the London Bullion Market Association
    - the Responsible Minerals Initiative
    - the Responsible Jewellery Council
    - the International Tin Supply Chain Initiative
    - the Dubai Multi-Commodities Centre
    - The Equator Principles.

Reference to existing guidance on how to address specific risks, such as:

- The gender chapter on integrating gender issues into due diligence in the OECD guidance for Responsible Business Conduct[1105]
- The UN Working Group on Business and Human Rights report on the gender dimensions of the Guiding Principles on Business and Human Rights[1106]
- The academic briefing on the need for business actors to undertake gender-responsive due diligence[1107]
- The European Commission Report on Critical Raw Materials and the Circular Economy[1108]
- The European Commission Report on the implementation of the Circular Economy Action Plan[1109]
- The Joint Ethical Trading Initiatives (ETI) Guide on Buying Responsibly.[1110]
- The Principles on Climate Obligations of Enterprises.[1111]
- The Children's Rights and Business Atlas.[1112]

Reference to indices and indicators such as:

[1104] Better Buying Initiative, available at: https://betterbuying.org.
[1105] OECD, "Due Diligence Guidance for Responsible Business Conduct" at 41.
[1106] UN Human Rights Council, above n868.
[1107] Bourke and Umlas above n868.
[1108] European Commission, "Report on Critical Raw Materials and the Circular Economy", Commission Staff Working Document, 16 January 2018, SWD(2018) 36 final.
[1109] European Commission, above n 932.
[1110] The Joint Ethical Trading Initiatives, "Guide to buying responsibly", available at: https://www.ethicaltrade.org/resources/guide-to-buying-responsibly.
[1111] Expert Group on Climate Obligations of Enterprises, *5 Principles on Climate Obligations of Enterprises* (Eleven International Publishing, 2018), available at: https://climateprinciplesforenterprises.files.wordpress.com/2017/12/enterprisesprincipleswebpdf.pdf.
[1112] Unicef, "Children's Rights and Business Atlas", available at: https://www.unicef.org/csr/businessatlas.htm.

- The Environmental Performance Index (EPI): which are metrics which score 180 countries based on their environmental performance;
- The Wage indicator;[1113]
- The Fair Trade price of relevant commodities or products.

7.2 Regulation of transnational corporate activity: foreign-based subsidiaries, suppliers and third parties

One of the problems perceived in the analysis of the study was that many of the human rights and environmental harms discussed take place outside of the EU within the subsidiaries or value chains of EU companies.

Parent companies and their (foreign) subsidiaries are traditionally treated as separate legal entities in matters relating to legal liability for harms caused. Whereas some financial other types of regulation applies to the entire corporate group,[1114] these do not ordinarily create civil liability for harms caused to third parties. Even where a parent company issues consolidated accounts for its foreign subsidiaries, it is seen as a separate legal entity from its subsidiaries in relation to damages caused. As a result of this limited liability, and as evidenced in the Regulatory Review, claimants are unable to take legal action against a corporate group or a parent company for harms caused by a foreign subsidiary, unless the cause of action is based on a failure of a duty by the parent company itself.

Similarly, suppliers and other third parties in the value chain are distincts legal entities.

In order to cover its intended reach, the regulation would need to require EU companies to undertake due diligence for harms caused by other enterprises within the corporate group, including foreign subsidiaries, as well as for the adverse impacts of activities within the supply and value chain.

It is noted that although the EU legal duty itself would only apply to companies linked to or operating in the EU, it would require these companies to undertake due diligence for those companies whose activities are included within the defined scope, including subsidiaries, suppliers and third parties in the value chain who are located in third countries. In turn, these non-EU entities would not themselves be bound by the EU law, but the adverse impacts of their activities would potentially need to be covered as part of the due diligence processes of their EU business partners.

The test as to how the legal scope should be defined would need to be considered. For example, a recent report by ClientEarth and Global Witness on EU-level mandatory due diligence to protect people and the planet suggests that the obligation could apply to all EU-based companies, or companies providing goods or services in the EU.[1115]

The EU and its Member States already regulate transnational corporate activities in various areas of law. Some of these regulations are not limited to subsidiaries or entities within the corporate group, or even to the supply or value chain, but extend to other actors such as agents, associated persons or branches.

Examples of how transnational corporate activity in the area of due diligence for responsible business conduct is currently regulated by the EU and in companies' home states are listed in the Regulatory Review as well as in **Table C.1** in **PART IV Annexure C: Application of EU and domestic law provisions to companies,** and include:

[1113] https://wageindicator.org.
[1114] Art 2(11) of Directive 2013/34/EU refers to the corporate group as a parent undertaking and all its subsidiary undertakings.
[1115] ClientEarth and Global Witness above n 163 at 14.

- The *domicile* of the defendant is the test used to determine both the scope of application of the Brussels I Recast Regulation and the place in which EU domiciled defendants are to be sued for civil liability claims. When the defendant is a company, the domicile is defined by Article 63 of the Regulation as the place where it has its *statutory seat, central administration or principal place of business*.

- The EU non-financial reporting requirement applies to relevant large public-interest companies *domiciled* in Member States,[1116] and uses the "business relationship" test to determine which impacts need to be covered in reports;

- The EU Conflict Minerals Regulation will apply to *importers* of tin, tantalum, and tungsten, their ores, and gold *into the EU*.

- The EU Timber Regulation applies to all operators *supplying* timber and timber products *in the EU*.[1117]

- The UK Modern Slavery Act applies to large companies *carrying on a business*, *or part of a business*, in any part of the United Kingdom.[1118] It requires companies to disclose the steps that they have taken to ensure that slavery and human trafficking is not taking place "(i) in any of its supply chains", and "(ii) in any part of its own business".

- The UK Bribery Act applies to companies *incorporated* under the law of any part of the United Kingdom, and applies to bribery activities *associated* with such companies that take place anywhere in the world.[1119]

- The French Law on the Duty of Vigilance applies to companies registered in France,[1120] and requires a standard of care for the activities with which the French company has an "established relationship";

- The Dutch Child Labour Due Diligence Law applies to companies *selling goods and supplying services* on the Dutch market.[1121]

- The Swiss Popular Initiative on Responsible Business purports to apply to companies that have their *registered office, central administration, or principal place of business* in Switzerland,[1122] and uses the "factual control" or "economic control"[1123] test to determine the scope of liability for due diligence.

- The Swiss counter-proposal uses instead the more limited "effective control" test which is based on accounting standards, and essentially extends liability for due

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[1116] EU Non-Financial Reporting Directive above n 24.
[1117] EU Timber Regulation above n 22.
[1118] Sections 54(2) and 54(12) of the UK Modern Slavery Act above n 30.
[1119] Section 7 of the UK Bribery Act above n 321.
[1120] Stéphane Brabant and Elsa Savourey, "Scope of the Law on the Corporate Duty of Vigilance: Companies Subject to the Vigilance Obligations", *Revue Internationale de la Compliance et de L'éthique des Affaires – Supplément à la Semaine Juridique Entreprise Et Affaires* No 50 (14 December 2017), available at: http://www.bhrinlaw.org/frenchcorporatedutylaw_articles.pdf.
[1121] The Netherlands Child Labour Due Diligence Act 2019.
[1122] SCCJ Initiative Text above n 493. While the scope of the Swiss Popular Initiative encompasses all Swiss-based companies, the scope of counter-proposal adopted by the National Council on 14 June 2018 is more restricted as it applies to Swiss-based companies exceeding two of the following three thresholds: a balance sheet total of 40 million CHF/USD; a turnover of 80 million CHF/US, or 500 full-time employees. See SCCJ "How does the parliamentary counter-proposal differ…" above n 493.
[1123] Under Art. 101a al. 2 lit.a Cst: Whether a company controls another is to be determined according to the factual circumstances. Control may also result through the exercise of power in a business relationship.

diligence to foreign subsidiaries only (rather than into the supply or value chain).[1124]

- The draft unofficial outline which is currently being discussed amongst stakeholders in Germany purports to apply to companies that have their *registered office, central administration, or principal place of business* in Germany.

Examples of how transnational corporate activity is currently regulated at EU level in other areas of law are set out in **Table C.2** in **PART IV Annexure C: Application of EU and domestic law provisions to companies**, and include:

- In EU competition law, a parent company can be liable for the infringement of EU competition law rules by its subsidiary when it exercises "*decisive influence*" over the conduct of such subsidiary, in which case both parent company and subsidiary are considered to form a "*single economic unit*" and therefore form a "*single undertaking*" within the meaning of Article 101 TFEU and are jointly and severally liable for the payment of the fine.[1125]

- Similarly, in EU Data Protection Law, a company can be liable for GDPR infringements of the entities over which it exercises a "*decisive influence*" so as to form a *single economic entity*, hence part of the same undertaking.[1126]

- In EU Anti-Money Laundering Directive, the Directive applies expressly to activities which took place outside of the EU. The Directive applies to institutions with *branches* in the EU, regardless of whether the head office is within the EU.[1127]

The above demonstrates that the regulation of transnational corporate activity is not at all unprecedented in the EU and its Member States, and is done in a variety of ways. One or a combination of these legal tests may be usefully copied for the application of the regulation. For example, in this case, the regulation could apply to companies registered, domiciled, or with their main place of business in an EU Member States, as well as those companies carrying out business or operating in the EU, including as subsidiaries, subcontractors and other business partners of non-EU companies.

The above examples also show that, in other areas of law, the level of factual influence exercised by the company is often determinative. Similarly, the concept of leverage is defined with reference to the level of influence which a company has over a third party. However, by using the "influence" or "control" tests to determine liability, a mechanism may incentivize companies to disengage from those activities in an attempt to remote itself from the scope of application. Instead, the concept of leverage actually expects companies to proactively engage more, and to demonstrate this engagement. In this way, a due diligence duty could utilize the legal test for "influence" or "control", by requiring companies to show that they have in fact exercised the expected amount of leverage to meet the due diligence standard.

7.3 Implementation at Member State level

[1124] The Swiss Initiative on Responsible Business aims to cover subsidiaries and economically controlled entities, whereas the counter-proposal is limited to legally controlled subsidiaries (and only when control is really exercised). See SCCJ "How does the parliamentary counter-proposal differ…" above n 493.
[1125] For example see *Akzo Nobel and Others v Commission* [2009] ECR I-8237.
[1126] EU GDPR above n 473 at 1–88.
[1127] Art 1(4) of the 4th EU Money Laundering Directive 2015/849 of the European Parliament and of the Council of 20 May 2015.

In accordance with Art 50 of the Treaty for the Functioning of the European Union and the TOR, it is anticipated that a legal duty which is formulated in European company law would most likely take the form of a Directive.[1128] In this way, the enforcement would take place within the individual legal systems of Member States, although the duty and its scope, including a requirement to provide for liability, would be established at EU level. It is noted that comparative EU regulation discussed in this study which take a similarly cross-sectoral approach, such as the EU Non-Financial Report Directive, also takes the form of a Directive.

Given the wide range of differences in the legal systems discussed in the Regulatory Review, the most effective implementation at Member State level would need to be considered in the design of any possible future EU intervention. It is noted that the two enforcement sub-options, relating to state-based oversight mechanisms and judicial or non-judicial remedies are *not mutually exclusive* and could both be created within the same instrument and operate simultanouesly in a complentary manner.

7.4 Material scope of adverse human rights and environmental impacts

One question which would need to be considered is the material scope of the due diligence duty to be created. In order to create legal liability, the material scope of the which kinds of impacts companies' due diligence would need to cover would have to be described with a certain degree of clarity, without limiting the open-endedness and flexibility of the general duty.

The UNGPs state that due diligence should cover "at a minimum" "all internationally recognized human rights".[1129] This is because business enterprises "may potentially impact virtually any of these rights."[1130] As evidenced elsewhere in this study, this is understood to include environmental impacts. The UNGPs list as "an authoritative list of the core internationally recognized human rights" those which are listed in the Universal Declaration of Human Rights, the International Covenant on Civil and Political Rights, the International Covenant on Economic, Social and Cultural Rights, and the principles concerning fundamental rights in the eight ILO core conventions as set out in the Declaration on Fundamental Principles and Rights at Work.[1131]

The phrase "at a minimum" is also important, as other international human rights treaties which are not included in this list but would nevertheless be commonly understood to constitute internationally recognized human rights. Examples include the Convention on the Rights of the Child, the Declaration on the Rights of Indigenous Peoples, Convention on the Rights of Persons with Disabilities, the Convention on the Elimination of all Forms of Discrimination Against Women.

Alternatively, an EU regulatory provision might require due diligence for "all EU-recognised human rights and environmental impacts", which is the definition provided for reference to stakeholders in the survey of this study. The question would be how this would be defined in cases where individual Member States have signed up to treaties which others have not signed. It is also noted that this would deviate from the UNGPs and the OECD Guidelines which refer to internationally-recognized human rights.

The French Duty of Vigilance Law applies to human rights and environmental harms without expressly defining the material scope of these harms. However, insofar as the

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[1128] A Directive is "a legislative act that sets out a goal that all EU countries must achieve. However, it is up to the individual countries to devise their own laws on how to reach these goals". Europa, "Regulations, Directives and other acts", available at: https://europa.eu/european-union/eu-law/legal-acts_en.
[1129] Commentary to UNGP 18.
[1130] Commentary to UNGP 18.
[1131] Commentary to UNGP 12.

UNGPs are expressly indicated as a justification for this law, it is expected that internationally recognized human rights and environmental standards may be applied.

Whilst the Swiss Responsible Business Initiative applies to internationally recognized human rights and environmental standards, the parliamentary counter-proposal is limited to the binding provisions under international law ratified by Switzerland.[1132]

An unofficial outline for a possible German draft law which is being considered by stakeholders refers to internationally recognized human rights, and defines this with reference to a list of international human rights treaties in an annex.[1133] An August 2019 study for the German Federal Ministry of Environment on the concept of environmental due diligence and how it could be applied as a legal requirement argues that for environmental due diligence "there is a lack of an international framework of reference similar to that for international human rights".[1134]

It is noted that an approach which simply requires due diligence for legal compliance with existing laws of the host (or home) state would not itself add any new legal obligations, as companies are in any event already required to comply with those laws of the countries where they operate. Moreover, such an approach would contradict the approach of the UNGPs which set out that the responsibility to respect "exists over and above compliance with national laws and regulations".[1135]

Another possibility would be that the duty would apply to "human rights and environmental harms" and that the material scope would be described in further detail in accompanying non-binding guidance. This is the approach followed in the French Duty of Vigilance Law.

7.5 Conflict of laws considerations

Under the general rule laid down in Article 4 of the Rome II Regulation, the applicable law which governs transnational civil liability claims is the law of the place where the damage occurred. With regard to transnational civil claims arising out of environmental damage or damage sustained to persons or property as a result of such damage, Article 7 of the Rome II Regulation provides that claimants can choose between the law of the place where the damage occured and the law of the country in which the event giving rise to the damage occurred.

Notwithstanding the exceptions to the general rule laid down in Article 4,[1136] and the special rules contained in the Rome II Regulation,[1137] the law of that host state will thus generally be the applicable law where the damage took place in a third country.[1138] However, as we have seen in the Regulatory Review, there is currently a general lack of

[1132] SCCJ "How does the parliamentary counter-proposal differ…" above n 493.
[1133] See above n 410.
[1134] Scherf et al above n 583 at 9.
[1135] Commentary to UNGP 11. See also UNGP 23.
[1136] Article 4 of the Rome II Regulation also provides for some exceptions according to which "where the person claimed to be liable and the person sustaining the damage both have their habitual residence in the same country at the time when the damage occurs, the law of that country shall apply" (Article 4.2); and " where it is clear from all the circumstances of the case that the tort/delict is manifestly more closely connected with a country other than indicated in paragraphs 1 or 2, the law of that other country shall apply" (Article 4.3).
[1137] These special rules concern in particular, product liability (Article 5), unfair competition and acts restricting free competition (Article 6), environmental damage (Article 7), infringement of intellectual property rights (Article 8), industrial action (Article 9), unjust enrichment (Article 10), negotiorum gestio (Article 11), culpa in contrahendo (Article 12) and the rules of safety and conduct (Article 17).
[1138] This is the case at the very least concerning civil liability claims arising out of human rights violations. The situation is more complex with regard to civil claims arising out of environmental damage for which, in theory at least, the law of the home state (i.e. the law of the place where the company is domiciled) could be applicable provided that the claimant can prove that the event giving rise originated from an action/inaction or decisions on the part of the parent or lead company. However, this can be very difficult to prove in practice. On this point see in particular Axel Marx, Claire Bright and Jan Wouters, "Access to Legal Remedies for Victims of Coporate Human Rights Abuses in Third Countries", 2019, available at: http://www.europarl.europa.eu/RegData/etudes/STUD/2019/603475/EXPO_STU(2019)603475_EN.pdf, at 118.

binding due diligence duties at national level both in EU member states and elsewhere. In addition, a recent study for the European Parliament on Access to justice for victims of corporate human rights abuses in third countries has shown that this constitutes a significant barrier to accessing legal remedies for claimants in civil proceedings arising out of alleged human rights abuses by EU companies in third countries.[1139] The study underlines in particular that "the effect of applying the law of the host state (as the law of the country in which the damage occurs) is often to deprive the victims of access to substantive justice and legal remedies".[1140]

The report highlights in this respect that:[1141]

> The possibility for the forum to apply its own law is confined to two mechanisms under the Rome II Regulation: the overriding mandatory provisions and the public policy exception. It has been argued that overriding mandatory provisions could be used to substitute the law of the forum (or part of it) for the law normally applicable when the latter is not sufficiently protective of the human rights of the victims. In addition, legislative provisions on mandatory due diligence such as the French Law on the Duty of Vigilance, could form the basis for overriding mandatory rules to ensure their applicability in civil liability cases relating to corporate human rights abuses in third countries. Moreover, the public policy exception could 'provide an important minimum guarantee (or "emergency brake") in foreign direct liability cases that are brought before EU Member State courts but governed by host country law, especially since fundamental human rights principles, whether ensuing from international or domestic law, are considered to be part of the public policy of the forum. These two exceptions provide, theoretically at least, the possibility for the forum state to apply its own law (at least in part) when the law of the host state does not offer enough protection for the human rights of the victims, or when damages in host countries are too low to deter businesses from further abuse. The Committee of Ministers of the Council of Europe has encouraged EU MS to make use of them. However, this possibility has not been confirmed in practice, and, in any case, their application is supposed to remain exceptional.

In order to address these issues, the study suggests that:[1142]

> A further choice of law provision be added to the Rome I Regulation. This provision would be specific to business-related human rights claims and allow the claimant to choose between the *lex loci damni*, the *lex loci delicti commissi* and the law of the place where the defendant company is domiciled in order to ensure more effective access to justice. This proposition would take into consideration the specific nature of the business-related human rights claims and redress the power imbalance between the parties, the victims usually being in a situation of particular vulnerability in relation to the multinational companies. It would also promote the interests of the respective countries and of the EU as a whole in upholding higher human rights standards. In this respect, it has been noted that 'the possibility of pursuing foreign direct liability cases in EU Member States on the basis of home country tort law is of fundamental importance. It determines whether EU MS can deploy their national rules in the field of civil liability as a much needed regulatory instrument to promote international corporate social responsibility and, more specifically, respect for human rights by EU-based enterprises operating in developing countries'. At the same time, it also determines the possibilities for host country based individuals and communities

[1139] Marx et al ibid at at 112.
[1140] Ibid at 113.
[1141] Ibid at 113.
[1142] Ibid at 114.

> who have suffered harm as a result of the activities of EU-based businesses with international operations to ensure, through this type of litigation, that the level or protection of their environmental and human rights interests is adequate and not fundamentally different from that afforded to those living in the EU home countries of the business enterprises involved'.

In case of a possible future EU intervention, consideration should be given as to how to ensure that the (newly created) EU standard of conduct for companies would be applied in EU member states' courts if the harm takes place in a third country. In line with the recommendations from the above-mentioned study, one option would be to indicate expressly that the provisions of the EU law should be considered as overriding mandatory provisions, and as such, applied regardless of the otherwise applicable law. Overriding mandatory provisions have been defined as:[1143]

> [P]rovisions the respect for which is regarded as crucial by a country for safeguarding its public interests, such as its political, social or economic organisation, to such an extent that they are applicable to any situation falling with their scope, irrespective of the law otherwise applicable to the contract under this Regulation.

This is the approach that has been taken in the Swiss Responsible Business initiative which states that its provisions "apply irrespective of the law applicable under private international law".[1144] Similarly, the unofficial outline for a German draft law discussed amongst stakeholders for due diligence in supply chains contains a provision to ensure the applicability of the due diligence duties on German companies in transnational civil liability claims irrespective of the foreign applicable law.[1145]

7.6 Transitional period

In the May 2018 European Parliament report on sustainable finance which forms the background to this study, it mentions a due diligence requirement which would apply "after a transitional period".[1146] As is evidenced in the Market Practices section, stakeholders have similarly referred to the usefulness of a transitional period, to allow time for companies to implement standards into practice. For example, the French Duty of Vigilance law allows for legal action to be taken only after the submission of reports for the financial year of 2018 (the first full financial year after the law came into force in early 2017). The Dutch Child Labour Due Diligence Law also provides for a transitional provision giving companies "five years to reduce or remedy any potential offending supply commitments entered into prior to the effective date of the Act".[1147]

Whereas it was highlighted that this may delay legal certainty provided by courts, some level of clarity about the implementation of the standard could be provided in the interim through non-binding guidance accompanying any legal duty.

7.7 Mandatory due diligence as part of a package of measures

Stakeholders indicated that mandatory due diligence legislation would need to be part of a "smart mix" of measures which would need to be implemented both by the EU and its

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[1143] Article 9 of Regulation (EC) No 593/2008 of the European Parliament and of the Council of 17 June 2008 on the law applicable to contractual obligations (Rome I).
[1144] SCCJ Initiative Text above n 493.
[1145] Norton Rose Fulbright, "Compliance update - Germany" (March 2019), available at: https://www.nortonrosefulbright.com/en-de/knowledge/publications/501f3fbf/compliance-update-germany.
[1146] European Parliament Report on Sustainable Finance, (2018/2007(INI)), available at: http://www.europarl.europa.eu/doceo/document/A-8-2018-0164_EN.html at para 6.
[1147] John Arvanitis and Kevin Braine, "Breaking Down the Dutch Child Labor Due Diligence Act" (2 July 2019), available at: https://www.kroll.com/en/insights/publications/dutch-child-labor-due-diligence-act.

Member States in order to have a greater impact.[1148] The UNGPs explicitly envisaged the need for states to consider a smart mix of measures and John Ruggie, the author of the UNGPs, reasserted this in a letter he recently wrote as a response to a public letter by Swiss business associations regarding their position on the Swiss Responsible Business Initiative that:[1149]

> Guiding Principle 3 and its extensive commentary emphasize that states are expected to adopt a mix of measures - voluntary and mandatory, national and international - to foster business respect for human rights in practice.

A recent report by Fern exploring the regulatory options for the EU in order to achieve sustainable cocoa supply chains also advocate for a "package of options to be implemented by the EU and its Member States".[1150] The report makes a number of suggestions in this respect, which could be extended beyond the cocoa sector, and include:

- The negotiation of bilateral agreements with producing countries, and the provision of financial and capacity-building assistance to achieve the agreed standards for production in the producer country and improve standards of governance and law enforcement.[1151]
- The development of "carding systems" through which the EU enters into dialogues with countries that export certain goods to the EU and issues yellow cards (warning) or red cards (import ban or notification of high risk) to those countries not combatting illegal behaviour in the supply chain, based on the EU Illegal, Unreported and Unregulated (IUU) Fishing Regulation.[1152]
- Setting expectations for Member States to use their public procurement policies in order to set incentives for companies in terms of human rights and environmental standards and promote responsible sourcing.[1153]
- Revising or clarifying EU competition law to "allow businesses greater freedom to collaborate for sustainability purposes, factor in externality costs and, in particular, discuss and address low prices paid to farmers".[1154]

Other measures could also include in particular:

- Setting expectations for Member States to establish clear guidelines for State-based financial institutions.
- Taking measures "to support producers in developing countries to improve their environmental standards and human rights practices and to improve livelihoods."[1155]

8. Discussion of strengths and weaknesses of the options identified

In the following, we discuss the perceived strengths and weaknesses of the options identified, in relation to one another and the no change / baseline scenario. These

1148 UNGP 3 and its commentary
1149 BHHRC, above n 854.
1150 Brack, above n 978 at 8.
1151 Ibid at 6.
1152 Ibid.
1153 Ibid.
1154 Ibid at 7.
1155 ClientEarth and Global Witness, above n 814 at 3.

strengths and weaknesses are based on the perceptions of stakeholders identified during the surveys and interviews, the country reports and the literature.

The following table elaborates for each option:

- Description of the option
- Strengths identified
- Weaknesses identified
- Relevant country examples
- Experiences at country level
- General conclusions

Regulatory Options Perceived Strenghts and Weaknesses

Option	Description	Strengths identified	Weaknesses identified	Relevant country and EU examples	Experiences at country level	Conclusions
1. No policy change	No changes in regulation at EU level for companies on undertaking due diligence through the supply or value chain. Expectation that legal developments around mandatory due diligence in Member States will continue.	No strengths identified.	Do not address the weakness of current legislative frameworks and the perceived need for action at the EU level (see Market Practices and Problem Analysis), with an increasing level of fragmentation of due diligence requirements across sectors, size of companies, countries and area of application Lack of legal certainty for businesses for requirements regarding supply chain due diligence.	See Regulatory Review.	See Market Practices and Problem Analysis.	No benefits identified / overall discontent with status quo.
2. New voluntary guidelines	New voluntary guidelines at EU level for companies on undertaking due diligence through the supply chain.	No strengths identified by majority of stakeholders.	Limitations in changing corporate practices. Multiplication of and confusion with existing and established voluntary guidelines. Continued fragmentation (as in Option 1). Lack of legal certainty, lack of level playing field for businesses.	Multiple, see Regulatory Review.	See Problem Analysis.	Limited perceived benefits / already enough voluntary guidance.

Option	Description	Strengths identified	Weaknesses identified	Relevant country and EU examples	Experiences at country level	Conclusions
3. New reporting requirement	New regulation at EU level requiring companies to report on the steps they have taken to identify, address, prevent and mitigate any adverse human rights and environmental impacts in their own operations or within the operations of third-party business relationships (including the supply or value chain).	Draws attention to issues within companies.	Limited impacts on corporate behaviour. No enforcement. No remedy. Continued fragmentation of standards that go beyond reporting. Lack of legal certainty for businesses regarding substantive requirements for supply or value chain due diligence that go beyond reporting.	EU Non-Financial Reporting Directive UK Modern Slavery Act 2015	Studies have shown that the impact of existing reporting requirements on corporate practices has remained very limited to date. Focus on material risks to company rather than risks to people and planet.	Some perceived benefits.
4. Mandatory due diligence	New regulation which requires companies to undertake mandatory due diligence in their own operations and through the supply or value chain.	Creates a level playing field, provides legal certainty, harmonisation, non-negotiable standard to increase leverage with third parties. Legal duty to incentivise implementation by companies.	Depends on sub-option, see below.	French Duty of Vigilance Law.	France: Study of the first vigilance plans suggests that they have focused on the risks to the business rather than the risks to other stakeholders. First legal actions brought, court decisions to clarify	Most perceived benefits indicated by stakeholders.

Option	Description	Strengths identified	Weaknesses identified	Relevant country and EU examples	Experiences at country level	Conclusions
		Potential access to remedy. Aligns with UNGPs and OECD Guidelines. (See Intervention Logic).			content of expectations.	
4.1 Applying only to certain sector(s)	Mandatory due diligence regulation would only apply to certain sectors.	Take into consideration the specificity of certain sectors.	Fails to protect against harms taking place outside of the sector(s). Fragmentation continues. Problematic for companies operating across sectors / sourcing from or business relationships with different sectors along value chain. Identification of "high risk" sectors problematic given presence of human rights and environmental risks in all sectors.	EU timber regulation EU conflict minerals regulation	EU Timber and Conflict Minerals Regulations: Different focus, related to imports and access to European market.	Overall stakeholder preference for cross-sectoral approach, which takes into account the specificities of the sector in its application.

Option	Description	Strengths identified	Weaknesses identified	Relevant country and EU examples	Experiences at country level	Conclusions
			Falls short of UNGPs due diligence which applies to all companies regardless of sector.			
4.2 Applying to companies across all sectors	Mandatory due diligence regulation would apply across all sectors	Provides general standard: Legal certainty and clarity Meets UNGPs: risks in all sectors	Enforcement to cover wide scope.	French Duty of Vigilance Law Dutch Child Labour Due Diligence Law	France: First legal actions brought against companies in variety of sectors.	Cross-sectoral approach preference of stakeholders overall.
4.2 (a) Applying to defined set of large companies only	Mandatory due diligence regulation would only apply to larger companies	Larger companies likely to have more resources and expertise to undertake due diligence. Due diligence of large companies would cover activities of small companies in their supply or value chain.	Falls short of UNGPs due diligence which applies to all companies regardless of size. Fails to cover small companies may also have severe impacts.	French Duty of Vigilance Law	France: First legal actions brought, some allegations relating to activities of subsidiaries and suppliers of large French companies.	Perception amongst small companies that large companies have more knowledge and resources for due diligence. Perception amongst large companies that small companies could pose severe risks and should be required to do due diligence.
4.2 (b) Applying to all companies regardless of size (including	Mandatory due diligence regulation would apply to all companies, including SMEs	Standard is context-specific so allows for priorisation of most	SMEs may not have the same resources as larger companies to undertake due diligence	UK Bribery Act 2010 Swiss	UK: Two thirds of SMEs had knowledge of UK Bribery Act,	Overall stakeholder preference for duty which applies regardless of size.

Option	Description	Strengths identified	Weaknesses identified	Relevant country and EU examples	Experiences at country level	Conclusions
SMEs)		severe risks; due diligence expectations determined by size, resources and risks. Aligns with UNGPs: SMEs may not have the same resources, but may have severe impacts.		counter-proposal (not yet law) applies to SMEs in "high risk" sectors.	knowledge highest with those aware of legal liability provisions.	
4.2(c): General duty applying to all business plus specific additional obligations only applying to large companies	General duty applying to all business, including SMEs, plus additional obligations only applying to large companies. The additional obligation is discussed with reference to the example of possible additional obligations for large companies relating to climate change.	Possible additional clarification of individual (large) companies' duties with respect to climate change due diligence.	Possible difficulty in distinguishing specific climate change due diligence obligations (applicable only to large companies) from those climate impacts that need to be considered as part of general duty.	EU non-binding guidance on climate-related information Dutch OECD National Contact point case Claims in terms of French Duty of Vigilance Law.	Extremely new developments.	Additional duty to be defined.
4.3	In order to be	Would contribute to	Need to set up	See two sub-	See two sub-	Necessary for duty

Option	Description	Strengths identified	Weaknesses identified	Relevant country and EU examples	Experiences at country level	Conclusions
Accompanied by oversight and/or enforcement	mandatory, due diligence regulation would be accompanied by an oversight and/or enforcement mechanism.	effectiveness of the regulatory regulation.	enforcement mechanism(s).	options below.	options below.	to be mandatory. Two sub-options not mutually exclusive, can operate together.
4.3 (a) Mechanisms for judicial and non-judicial remedies	Mandatory due diligence regulation would be accompanied by mechanisms for judicial and / or non-judicial remedies	Would provide remedy for victims. No need to set up a State-based oversight body.	Burden on public courts and other bodies involved in remediation. Burden on companies and affected right-holders to use mechanisms for judicial and non-judicial remedies. Other barriers to access to remedy (costs, legal representation) may result in low number of claims.	French Duty of Vigilance Law Dutch Child Labour Due Diligence Law	France: First legal actions instituted. Netherlands: New law not yet enforced.	Benefit of providing remedy to victims, identified by stakeholders as key shortcoming of status quo.
4.3 (b) State-based oversight body and sanction for non-compliance	Mandatory due diligence regulation would be accompanied by a State-based oversight body and sanction for non-compliance.	Level playing field depending on enforcement.	Need to set up oversight and/or enforcement mechanism. Potential need to oversee due diligence of all (large) companies: may be under-resourced, leading to limitations in	UK Bribery Act 2010 Dutch Child Labour Due Diligence Law	UK: Bribery Act perceived to be effective to drive due diligence practices despite low number of prosecutions and resources.	Potentially effective to incentivise implementaiton, but costly. Fines paid by companies may offset costs involved.

Option	Description	Strengths identified	Weaknesses identified	Relevant country and EU examples	Experiences at country level	Conclusions
			effectiveness. Does not provide remedy for those affected.			

V ASSESSMENT OF OPTIONS

The assessment of regulatory options was undertaken by LSE Consulting, and in particular by Matthias Bauer, Hanna Deringer, Daniela Baeza-Breinbauer, and Francisca Torres-Cortés.

1. Literature Review

The following section reviews existing impact assessments on similar legislative initiatives, studies, reports and academic literature to provide an overview of results from other studies which can inform the assessment of costs and benefits of the regulatory options at issue. The literature review covers potential economic impacts on companies (costs and benefits), company-level competitiveness and SMEs in particular. Moreover, it provides a review of existing studies on social and environmental impacts, impacts on human rights as well as public administrations in the EU and its Member States.

1.1 Economic Impacts

The objective of the economic impact assessment is to quantify economic impacts of the proposed regulatory options as far as possible in order to enable the comparison between economic costs and economic benefits resulting from a new regulation. However, as the literature review demonstrates, it is not always possible to provide reliable quantitative estimates for all types of costs and benefits which need to be considered and discussed. Quantitative estimates are primarily available for economic costs of individual companies. In contrast, while there is also evidence regarding the expected benefits for companies resulting from sustainability measures, these are generally more difficult to quantify in terms of their magnitude. Apart from the company-level impacts, which provide the basis for the estimations of economic costs and benefits, we also review potential impacts on company-level competitiveness, impacts on SMEs in particular and conclude by discussing industry and economy-wide economic impacts.

1.1.1 Company-level Costs

The French Duty of Vigilance Law, which is the leading example of a law requiring due diligence as a standard of care for human rights and environmental harms as set out in the mandate for this study, has not been in force for long enough to have generated information regarding implementation costs for companies. However, company-level impact assessments covering various aspects that are related to the subject of this impact assessment are available for the EU Timber Regulation, EU's Non-financial Reporting Directive, the EU Conflict Minerals Regulation, and Section 1502 of the US Dodd-Frank Act (US DFA). While the EU's Non-financial Reporting Directive is primarily about the disclosure of certain non-financial information, both the US and the EU conflict minerals and timber policies include due diligence procedures for relevant suppliers as well as several disclosure obligations. The major features and legal obligations of these regulations, e.g. data collection, disclosure and reporting requirements, are outlined in Table 0.1.

These comparative impact assessments as considered as a result of the absence of sufficient evidence relating to the impacts of the French Duty of Vigilance Law. However, the particular relevance of impacts of these other laws should be understood as being limited insofar as they contain legal duties which are different in nature to due diligence is a standard of care as envisioned in the French Duty of Vigilance Law, which informs the mandate of this this study.

Table 0.1: Major features and legal obligations of related regulations

Law/regulation	Legal requirements for companies
EU Timber Regulation[1156]	The **EU Timber Regulation (EUTR)** came into force in March 2013. It aims to reduce illegal logging by ensuring that no illegal timber or timber products can be sold in the EU. It applies to wood and wood products being placed for the first time in the EU market, and defines 'legal' as timber produced in compliance with the laws of the countries where it is harvested. The 28 EU Member States are responsible for laying down effective, proportionate and dissuasive penalties and for enforcing the regulation.[1157] The EUTR sets out three key obligations: • Placing illegally harvested timber products derived from such timber on the EU market for the first time, is prohibited. • EU operators – those who place timber products on the EU market for the first time – are required to exercise due diligence. • Traders – those who buy or sell timber and timber products already on the market – are required to keep information about their suppliers and customers to make timber easily traceable. Operators can develop their own due diligence systems or use one developed by a monitoring organisation.[1158] The regulation defines due diligence based on three elements: • Information – Operators must have access to information describing the timber and timber products, including details of their origin, suppliers, and information on compliance with national legislation. • Risk assessment – Based on the information identifies above and the criteria set out in the regulation, operators should assess the risk of illegal timber in their supply chains. • Risk mitigation – When the assessment shows that there is a risk of illegal timber in the supply chain, that risk can be mitigated by requiring additional information and verification from the supplier.
EU Non-financial Reporting Directive[1159]	This EU Directive requires large companies to disclose certain information on the way they operate and manage social and environmental challenges. EU rules on non-financial reporting only

[1156] Timber Regulation (2010), Regulation (EU) 995/2010 of the European Parliament and of the Council of 20 October 2010 laying down the obligations of operators who place timber and timber products on the market. Available at: https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:32010R0995&from=EN

[1157] DG Environment. (2019). Timber Regulation. [online] Available at: https://ec.europa.eu/environment/forests/timber_regulation.htm

[1158] DG Environment. (2013). What does the law say? - EU timber regulation 2013. [online] Available at: https://ec.europa.eu/environment/eutr2013/what-does-the-law-say/index_en.htm

	apply to large public-interest companies with more than 500 employees. This covers approximately 6,000 large companies and groups across the EU, including listed companies, banks, insurance companies and other companies designated by national authorities as public-interest entities. Under Directive 2014/95/EU, large companies have to publish reports on the policies they implement in relation to environmental protection, social responsibility and treatment of employees, respect for human rights anti-corruption and bribery, diversity on company boards (in terms of age, gender, educational and professional background). Directive 2014/95/EU gives companies significant flexibility to disclose relevant information in the way they consider most useful. Companies may use international, European or national guidelines to produce their statements. Since 2017, voluntary guidelines by the EC exist on how to disclose environmental and social information.[1160]
EU Conflict Minerals Regulation[1161]	**EU importers of tin, tantalum, tungsten and gold** must check what they are buying, to ensure it has not been produced in a way that funds conflict or other related illegal practices.[1162] The regulation **requires importers to follow a five-step framework** which the Organisation for Economic Co-operation and Development (OECD) has laid out in a document called 'Due Diligence Guidance for Responsible Supply Chains from Conflict-Affected and High-Risk Areas' (OECD Guidance). These steps require an importer to: **1.** **ESTABLISH STRONG COMPANY** MANAGEMENT SYSTEMS **2.** **IDENTIFY AND ASSESS RISK IN THE SUPPLY CHAIN** **3.** **DESIGN AND IMPLEMENT A** STRATEGY TO RESPOND **TO IDENTIFIED RISKS** **4.** **CARRY OUT AN INDEPENDENT** THIRD-PARTY AUDIT **OF SUPPLY CHAIN DUE DILIGENCE** **5.** REPORT ANNUALLY **ON SUPPLY CHAIN DUE DILIGENCE**
Section 1502 of the US Dodd-Frank Act (US DFA)[1163]	The US Conflict Minerals Act (Section 1502) in the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act requires **US registered companies** to disclose whether the minerals they source

[1159] Non-financial Reporting Directive (2014). Directive 2014/95/EU of the European Parliament and the Council of 22 October 2014 amending Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups. Available at https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014L0095&from=DE
[1160] Commission guidelines on non-financial reporting. Available at https://ec.europa.eu/info/publications/170626-non-financial-reporting-guidelines_en
[1161] Conflict minerals Regulation (2017). Regulation (EU) 2017/821 of the European Parliament and of the Council of 17 May 2017 laying down supply chain due diligence obligations for Union importers of tin, tantalum and tungsten, their ores, and gold originating from conflict-affected and high-risk areas. Available at https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32017R0821&from=DE
[1162] European Commission (2019). The regulation explained. Available at http://ec.europa.eu/trade/policy/in-focus/conflict-minerals-regulation/regulation-explained/
[1163] The US Conflict Minerals Act (Section 1502) in the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act requires US registered companies to disclose whether the minerals they source originate from the Democratic Republic of Congo or its neighbouring countries. The four minerals from DRC mines or adjoining countries defined as “conflict minerals” in Section 1502(e)(4) of the Act are cassiterite (tin), columbite-tantalite (tantalum) and wolframite (tungsten) – also referred to as the “3Ts” and gold. Companies that manufacture products containing these conflict minerals are required to document if any 3TG in their products have been purchased from Covered Countries where armed groups are suspected of committing human rights violations.

originate from the Democratic Republic of Congo or its neighbouring countries.[1164] The goal of the law is to **provide transparency of material origin** and allow customers to make purchasing decisions based on that information. The three-step procedure to be followed is:

6. ASSESSMENT WHETHER CONFLICT MINERALS ARE NECESSARY **TO FUNCTIONALITY OR PRODUCTION OF PRODUCTS MANUFACTURED IN THE REPORTING YEAR,**

7. **CONDUCTING A** REASONABLE COUNTRY OF ORIGIN INQUIRY **TO DETERMINE WHETHER ANY ORIGINATE IN THE DEMOCRATIC REPUBLIC OF CONGO OR ADJOINING COUNTRIES,**

8. **IF SO,** CONDUCTING SUPPLY CHAIN DUE DILIGENCE **IN ACCORDANCE WITH INTERNATIONALLY RECOGNISED DUE DILIGENCE FRAMEWORK AND ISSUE A CONFLICT MINERALS REPORT (CMR)**

As concerns the company-level costs and administrative burden, the impact assessments of these policies have some commonalities, but also show differences in the methodologies applied by the authors. The studies' shortages generally include a lack of publicly available industry data and a high variation in the quantitative and qualitative information collected through surveys and consultations. Therefore, the figures provided should be considered as broad estimates and the results should be interpreted with caution.

Regarding the studies' commonalities, numerical cost estimates are usually provided for one-time costs resulting from preparatory measures needed to comply with the regulations as well as recurrent costs. Costs are usually expressed in annual numbers on a per company basis. Some studies aggregate these numbers to arrive at a total cost for all companies affected by the respective regulation.

One-time costs usually include internal staff cost, fees for external advisory services and costs related to changes in ICT systems and procedures. Recurrent costs include staff costs related to the collection of required information, the preparation of reports, the verification of information, the disclosure of information, and/or the publication of reports. In addition, fees for external consultants as well as costs of external auditors feed into the estimation of regulation-induced recurrent costs.

Cost estimates are either taken from the companies' replies gathered through consultations and surveys or estimated by multiplying a given number of working hours required (usually stated by the business respondents) and labour costs per hour (usually based on available industry intelligence), depending on the administrative procedures prescribed by the intended regulation.

While the impact assessment for the obligations from Section 1502 of the US Dodd-Frank Act focuses on specific legal obligations, the EU's assessments of the economic impact of the Non-financial Reporting Directive and the Conflict Minerals Regulation

[1164] Thousands of manufacturers – ranging from Fortune 500 companies to companies with 10 million USD in annual sales – in the industrial, aerospace, healthcare, automotive, chemicals, electronics/high tech, retail, and jewellery industries are consumers of these metals. All these companies are affected by the new law. See also OECD (2016). Quantifying the Costs, Benefits and Risks of Due Diligence for Responsible Business Conduct Framework and Assessment Tool for Companies- June 2016. Available at https://mneguidelines.oecd.org/Quantifying-the-Cost-Benefits-Risks-of-Due-Diligence-for-RBC.pdf analyse different policy scenarios and options respectively. A brief explanation of the methodologies applied in the assessments of the EU Timber Regulation, the EU Non-financial Reporting Directive and the EU Conflict Minerals Regulation as well as a break-down of the analysed options is provided in Table 8.1. These studies are relevant examples or due diligence-related assessments that consider policy options that gradually increase obligations for the different stakeholders aiming to strengthen positive effects on CSR practices, human rights and the environments.

Table 8.1: Overview of options analysed in relevant EU impact assessments

Methodology for the assessment of the economic impact of the EU Timber Regulation[1165,1166]	Methodology for the assessment of the economic impact of the Non-financial Reporting Directive[1167]	Methodology for the assessment of the economic impact of the EU Conflict Minerals Regulation[1168]
The study estimated the average costs of a legality control system through country case studies considering three different stages within the supply chain. Secondly, it analysed the potential shifts of trade flows from one region to another and the impact on prices of wood and wood products using a partial equilibrium model for forest and forestry industries. Additionally, the estimated environmental impacts in terms of the change in the volume of illegal logging. The study analysed 6 policy options; the baseline option is the no policy-change scenario and the other options would be added up to that scenario: • Baseline/minimum option – implementation of the Voluntary Partnership Agreements, a licensing scheme that provides more certainty to EU operators and six timber producing countries. • Additional option 1 – Expanded coverage of the bilateral approach through FLEGT VPAs to 6 additional countries. • Additional option 2 – Further development of	The initial impact assessment from 2014 focuses on the effects of improved disclosure of non-financial information by EU companies as part of a broader set of EU initiatives on CSR. The assessment is accompanied by a study prepared by the Centre for Strategy and Evaluation Services, which provides a qualitative analysis of current non-financial reporting practices as well as a cost/benefit assessment based on a survey. In this study, the following methodology is applied. The study analyses 3 policy options: • **Option 1** – Requires a statement in the Annual Report, i.e. possibility of strengthening the existing requirement to disclose a statement on non-financial information in the Annual Report. • **Option 2** – Requirement of a Detailed Report, with sub-option for mandatory reporting and different reporting obligations. • **Option 3** – Mandatory EU Standard, which would constitute a framework for disclosing non-financial information.	The study quantifies the compliance costs for businesses subject to an EU responsible sourcing initiative. The authors combine qualitative assessments with quantitative methods. It is recognised that the study, like similar studies, suffers from data limitations. The study consists of two main parts: the first part provides a description of global supply chains and trends for relevant commodities. The second part outlines the results of a comprehensive user survey. The analysis is supplemented by related literature, databases and industry intelligence. The cost estimates given by the study are based on the survey results. The authors distinguish between two cost types: initial costs, e.g. one-time efforts for companies to be able to comply with conflict minerals reporting, and ongoing costs of compliance. The authors highlight that many respondents indicated only very rough estimates. Some stated that cost estimates were not possible at the time of the survey. One survey participant indicated very high costs, while many others indicated much lower costs. A distinction was made between SMEs and large enterprises with 250 and more

[1165] See COMMISSION STAFF WORKING DOCUMENT Accompanying document to the Proposal for a Regulation of the European Parliament and the Council determining the obligations of operators who make timber and timber products available on the Market. IMPACT ASSESSMENT Report on additional options to combat illegal logging. Available at: https://ec.europa.eu/environment/forests/pdf/impact_assessment.pdf

[1166] Indufor (2008). *Assessment of the impact of potential further measures to prevent the importation or placing on the market of illegally harvested timber or products derived from such timber*. Final Report. [online] Helsinki, Finland: Indufor in association with European Forest Institute (EFI). Available at: https://ec.europa.eu/environment/forests/pdf/ia_report.pdf [Accessed 10 Sep. 2019].

[1167] See COMMISSION STAFF WORKING DOCUMENT IMPACT ASSESSMENT Accompanying the document Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL amending Council Directives 78/660/EEC and 83/349/EEC as regards disclosure of non-financial and diversity information by certain large companies and groups. Available at https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52013SC0127.

[1168] See European Commission (2014), Impact Assessment Accompanying the document Proposal for a Regulation of the European Parliament and of the Council setting up a Union system for supply chain due diligence self-certification of responsible importers of tin, tantalum and tungsten, their ores, and gold originating in conflict-affected and high-risk areas. PART 3 (see first part of Annex III to the Impact Assessment). Full external report available at https://publications.europa.eu/en/publication-detail/-/publication/dced6d04-92fb-4a20-a499-4dad9974aee7 01aa75ed71a1.0001.01/DOC_3&format=PDF.

voluntary measures by the private sector, such as codes of conduct and forest certification schemes.

- Additional option 3 – Broder measures to prevent the importation of illegally harvested timber by declaring it illegal regardless of the level of risk in trading.
- Additional option 4 – Prohibition on the placing on the EU market of illegally harvested timber, including imported forest products and those produced in the EU.
  - Sub-option 4A – Prohibition on trading and possession of timber and timber products harvested in breach of the laws of the country of origin.
  - Sub-option 4B – Requiring that only legally harvested timber and timber products to be placed on the market.
- Additional option 5 – Legislation which requires due diligence by all timber traders to ensure that they trade in legally harvested timber.

employees. In addition, publicly traded companies, which have different reporting requirements, have been analysed separately. Additional questions were raised about the impact on local operators, e.g. expected 'economic losses for local operators', 'cost or price increases', 'increased illegal trade and corruption'.

The study analyses 6 policy options:

- **Option 1** – Standalone EU Communication
- **Option 2** – 'Soft-law' approach combining option 1 with a Council Recommendation.
- **Option 3** – Regulation establishing obligations under an 'EU responsible importer' certification based on OECD Guidance – VOLUNTARY. The Regulation relies on the OECD Guidance to define obligations for EU importers that opt to be self-certified as responsible importers of tin, tantalum and tungsten ores and metals, and gold, on the basis of a self-declaration of compliance.
- **Option 4** – Regulation establishing obligations under an 'EU responsible importer' certification based on the OECD Guidance – MANDATORY. This option combines the measures described under Option 1, with a compulsory version of the Regulation described in Option 3 under which all EU importers of tin, tantalum and tungsten ores and metals, and gold, would be subject to the obligations defined under the Regulation.
- **Option 5** – Directive establishing obligations for EU-listed companies based on the OECD Due Diligence Guidance. This option combines the measures described under Option 1, with a Directive targeting almost 1,000 EU-listed companies using tin, tantalum, tungsten and

		gold, regardless of origin, in their supply chain. • **Option 6** – Prohibition of imports when EU importers of ores fail to demonstrate compliance with OECD Guidance) – import ban. This option consists of the measures described under Option 1, and in addition it would require EU importers to mandatorily demonstrate compliance with the OECD Guidance. Providing evidence on compliance to Member States' customs authorities, importers will be eligible to access the EU market.

Annexure 4 provides the results of the studies displayed in Table 1.2. Depending on the methodology chosen by the respective authors, cost estimates are provided for (**see PART IV Annexure D** for more details on the different types of company-level costs):

- One-time costs related to changes to corporate compliance policies (see Annexure D, Table 1)
- One-time costs for the set-up and operation of necessary IT systems (see Annexure D, Table 2)
- Recurrent costs related to audits (see Annexure D, Table 3)
- Recurrent costs for data collection, e.g. verifications that suppliers are providing credible information (see Annexure D, Table 4)
- Recurrent costs of filing necessary forms (see Annexure D, Table 5)
- Total first-year costs (see Annexure D, Table 6)
- Total recurrent costs in the following years (see Annexure D, Table 7)

It should be noted that the cost estimates per type of cost vary, sometimes significantly, depending on information gathered from individual companies, differences in hourly labour cost estimates and the way final numbers have been aggregated.

At least five different studies are available for the assessment on the economic impacts of Section 1502 of the US Dodd-Frank Act, implying that these studies' results can be checked against each other for robustness. Studies other than those commissioned by the European Commission are not available for the economic impacts of the EU's due diligence policies. Accordingly, as indicated by Bayer and de Buhr for the assessment of the impact of Section 1502 of the US Dodd-Frank Act, the EU studies may over- or underestimate the impact of the regulations analysed by the authors.[1169]

Most studies provide ranges of estimates for different types of costs and different sizes of companies, e.g. large companies versus SMEs or companies whose revenues exceed certain revenue thresholds.

A relatively detailed break-down of cost estimates is given in the economic impact assessment of the EU's Non-financial Reporting Directive, which, however, does not provide for detailed value chain due diligence requirements.

Table 8.2 provides a summary of the costs by company for different costs types as estimated for the EU's Non-financial Reporting Directive [1170,1171]. For large companies, the cost burden is estimated to range from 155,000 to 604,000 EUR. For SMEs, the cost burden is estimated to range from 8,000 to 25,000 EUR per company and year. It should be noted though that the costs listed in the study only relate to companies' reporting activities, not to due diligence activities. For example, no costs are listed for companies' engagement with suppliers, code of conduct drafting and compliance monitoring, creating and implementation of human rights policies, grievance mechanisms, or remediation.

[1169] Bayer and de Buhr, C. 2011. A Critical Analysis of the SEC and NAM Economic Impact Models and the Proposal of a 3rd Model in view of the Implementation of Section 1502 of the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act. LA: Tulane University. Available at https://lawprofessors.typepad.com/files/tulane-study.pdf

[1170] European Commission (2013). COMMISSION STAFF WORKING DOCUMENT IMPACT ASSESSMENT Accompanying the document Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL amending Council Directives 78/660/EEC and 83/349/EEC as regards disclosure of non-financial and diversity information by certain large companies and groups. Available at https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52013SC0127

[1171] OECD (2016). Quantifying the Costs, Benefits and Risks of Due Diligence for Responsible Business Conduct Framework and Assessment Tool for Companies- June 2016. Available at https://mneguidelines.oecd.org/Quantifying-the-Cost-Benefits-Risks-of-Due-Diligence-for-RBC.pdf

These numbers need to be contrasted with assessments that have been conducted by business associations: A study from the Confederation of British Industry (CBI 2013) estimates cost of 30,000 GBP per company (approximately 40,000 EUR as of 2011) in the first year. In addition to these numbers, according to the OECD (p.23) "[t]he French business submission to the EC Consultation on non-financial reporting reported costs between 50,000 and 200,000 EUR per company for data collection, internal processing and consolidation; 50,000 to 100,000 EUR for data publication in the management report; and the largest cost (between 100,000 and 750,000 EUR) for external verification of reporting processes (mandatory in France as of 2012) and of CSR data (on a voluntary basis), adding up to total annual costs per company between 200,000 and over 1 million EUR." [1172]

Table 8.2: Summary of the costs by company for different costs types as estimated for the EU's Non-financial Reporting Directive[1173]

	Large Companies	SMEs
Training costs	Up to 18 days (often also no training or training on the job) Up to 5,000 EUR	n/a
Collection of New Data (internal staff)		
Days	35 to 100 days	n/a
Cost	227 EUR per day: 8,000 EUR and 23,000 EUR	n/a
Report Drafting (internal staff)		
Days	80 to 480 days	15-20 days
Cost	Costed at 227 EUR per day: Between 18,000 and 109,000 EUR	Cost at 227 EUR per day: Between 3,000 and 5,000 EUR
Report Design (usual external cost)	Between 10,000 and 100,000 EUR	Between 1,000 and 2,000 EUR
Report processing (external cost)	Up to 97,000 EUR	Under 20,000 EUR
Report Publication (depending on publishing strategy – internet or printed)		
Days	2 to 50 days	2 days
Cost	Between 1,000 to 192,000 EUR (printed version) Between 10,000 and 35,000 EUR (online) Overall: Between 1,000 and	Under 1,000 EUR

[1172] Ibid.
[1173] CSES (2011). Framework Contract for Evaluation and Impact Assessment activities of Disclosure of non-financial information by Companies. Final report. Centre for Strategy and Evaluation Services, UK. Available at http://ec.europa.eu/finance/accounting/docs/non-financial-reporting/com_2013_207-study_en.pdf. And OECD (2016).

	131,000 EUR	
External Assurance/Audit	Between 22,000 and 114,000 EUR	n/a
TOTAL		
Days		
Cost	Between 155,000 and 604,000 EUR	Between 8,000 and 25,000 EUR

Available impact assessments indicate that the potential financial cost burden of reporting requirements varies widely across companies depending on size, value-chain complexity and other sector characteristics.

As concerns the overall cost magnitude of the administrative burden, available studies demonstrate that the concrete cost impact critically depends on how costly it is for companies to set up additional resources and new organisational procedures to comply with the regulations. For example, the estimated total cost impact resulting from the EU's Conflict Minerals Regulation is found to be much lower than the cost impact estimated for US companies that have to comply with the US' conflict minerals policies. An explanation might be that the EU's regulation targets only upstream supplies such as smelters and refiners, while the US regulations require a much more diverse range of publicly listed companies to check and report on their supply chains. For the latter group, according to the impact assessments, complying with the (then new) regulations turned out to cause much higher additional costs than for companies that have close affiliations with minerals suppliers. Another explanation might be that the US law is more strictly enforced through the US Securities and Exchange Commission (SEC). As a result, the stakes might be higher for US companies, incentivising them to take more actual due diligence steps, which result in higher costs.

As reporting, data collection and auditing requirements are different for all three regulations, it is generally difficult to compare the overall impact of these requirements. The studies' results suggest, however, that the administrative burden resulting from the reporting requirements of the EU's Non-Financial Reporting Directive is in many cases higher than the cost burden estimated for the US conflict minerals regulations, and substantially higher than the cost burden estimated for the EU Conflict Minerals Regulation. Depending on the coverage required by the laws, the cost burden of the verification of information collected from third parties can lead to a substantial cost burden (as, for example, indicated by the French business submission to the EC Consultation on non-financial reporting).[1174]

Based on the impact assessments available, it is generally difficult to objectively assess the proportionality of the measures (and options) analysed as pecuniary estimates are not available for the benefits of the measures. As concerns the magnitude of the cost impact of the proposed measures, the compliance costs generally increase with the legal requirements (demands) of the regulation. The impact assessments also stress that companies not directly affected by the regulations are likely to be impacted indirectly

[1174] OECD (2016). Quantifying the Costs, Benefits and Risks of Due Diligence for Responsible Business Conduct Framework and Assessment Tool for Companies- June 2016. Available at https://mneguidelines.oecd.org/Quantifying-the-Cost-Benefits-Risks-of-Due-Diligence-for-RBC.pdf

through supply chain effects. Quantitative estimates for these 'second rounds' effects are, however, missing in these studies.

1.1.2 Company-level Benefits

In order to compare the expected costs for EU companies from the proposed regulatory options with the possible economic benefits resulting from such policies, a comprehensive literature review has been conducted to review existing studies which assess and estimate the potential economic benefits. Due to the lack of studies which focus specifically on due diligence for human rights and environmental harms, such as contained in the French Duty of Vigilance Law, the review covers mainly studies which refer to general concepts such as sustainability reporting or corporate social responsibility (CSR) activities or studies which use environmental, social, and governance (ESG) performance as an indicator. Furthermore, it is also important to point out that most studies assess business practices rather than impacts from regulations and laws. We note that the impacts of due diligence practices may not be identical to the impacts of due diligence laws and that they would only be comparable if a law or regulation would lead to the same business practices. In the absence of studies which assess specifically impacts from similar regulations and laws, the results from these general studies will be used as far as possible for the assessment of the different regulatory options in this assessment, but accompanied by a critical discussion of their suitability and appropriateness.

In general, it is difficult to find studies, which quantify the magnitude of the economic benefits of the companies' sustainability activities. The main reason for this is the fact that it is difficult to relate specific economic benefits directly to the assessed sustainability activities. For the cost side, this is generally easier to accomplish since a particular activity causes a specific cost, but the reasons for an economic benefit that a company experiences may be manifold. A benefit, such as improved financial performance or increased operational efficiency, may be the result of a complex mix of factors, either different CSR or ESG activities, other activities of a company or other external factors which influence the economic performance of companies. In this regard, an OECD study states that it is extremely difficult to isolate the effects of one responsible business conduct measure from another since these tend to create multiple intermediate effects that play into each other.[1175]

The literature review will outline the main studies we found regarding the positive economic impacts of CSR and ESG activities on a company-level. It covers the main economic benefits that can result for a company from sustainability measures according to the reviewed surveys and studies. For sector-specific impacts these results can be used when adapted to the specificities of the studied sector. For example, in some more sensitive sectors measures regarding sustainability, due diligence or risk management seem to be of higher importance than in less sensitive sectors for the purposes of avoiding higher risks.

Different types of benefits

[1175] Ibid.

Several studies, mainly surveys, have been conducted to assess the main economic benefits companies expect from sustainability reporting and CSR activities. One main meta-study reviews academic literature and business reports and conducts an analysis of empirical data from the Business in the Community Ireland (BITCI) for the years 2003 to 2010. The study identifies more than 60 possible business benefits and indicates the following seven benefits as the most important benefits (i.e. based on the frequency of citation) for companies[1176]:

1) Brand value and reputation
2) Employees and future workforce
3) Operational effectiveness
4) Risk reduction and management
5) Direct financial impact
6) Organisational growth
7) Business opportunity

In addition, a number of consulting reports from large consulting companies have assessed, mainly based on surveys, the potential benefits that companies expect from their sustainability activities.

A large report from Ernst & Young and the Boston College Centre for Corporate Citizenship discusses the different benefits that arise for companies from sustainability reporting based on a survey conducted among 579 companies on their sustainability reporting. The survey results indicate that companies consider the following aspects as the main benefits from sustainability reporting (by order of relevance): improved reputation (>50% of respondents), increased employee loyalty, reduction of inaccurate information on the company's social performance, refinement of corporate vision or strategy, increased consumer loyalty, waste reduction within company, better relationship with regulatory bodies, better monitoring and improvement of long-term risk management, cost savings within company, increased long-term profitability, better access to capital, and better insurance rates.[1177]

A large business survey conducted by McKinsey in 2017 among 2,700 companies across different regions, company sizes and industries on their sustainability programs addressing environmental, social, and governance issues revealed similar views. The top eight reasons why companies address sustainability matters were (by order of relevance): the company's goals, mission or values; its reputation; consumer expectations; new growth opportunities; operational efficiency; regulatory requirements; economic growth; employee satisfaction and attraction.[1178]

KPMG conducts regular surveys on corporate responsibility reporting. The 2011 report assesses the reasons for companies to report on their corporate responsibility activities. It stands out in terms of the number of companies covered as it bases its findings on 3,400 companies from 34 countries, which include the largest 250 global companies. The results suggest that companies view the following aspects (in order of relevance) as the

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[1176] Exter, N. and Cunha, S. and Turner, C. (2011) The business case for being a responsible business, Doughty Centre for Corporate Responsibility at the Cranfield School of Management. Available at https://dspace.lib.cranfield.ac.uk/bitstream/handle/1826/8298/The_business_case.pdf?sequence=1&isAllowed=y
[1177] Ernst & Young and the Boston College Centre for Corporate Citizenship (2016). Value of sustainability reporting Value of sustainability reporting. A study by EY and Boston College Center for Corporate Citizenship. Available at https://de.scribd.com/document/282949295/EY-Value-of-Sustainability-Reporting
[1178] McKinsey (2017) Sustainability's deepening imprint. Available at: https://www.mckinsey.com/business-functions/sustainability/our-insights/sustainabilitys-deepening-imprint#

eight most important drivers – and thus expected potential benefits – behind their activities: brand reputation, ethical considerations, employee motivation, innovation and learning, risk management and risk reduction, access to capital or increased shareholder value, economic considerations, better supplier relationships.[1179]

Another report from Ernst & Young summarises key messages from supply chain, procurement and sustainability executives from 70 companies in order to discuss the drivers, approaches and challenges companies face in the ongoing journey to building a responsible and resilient supply chain. As the main benefits for companies from improving environmental, social and governance (ESG) performance in their supply chains, the study names improved processes, reduced costs, increased productivity, innovation, and improvement of societal outcomes.[1180]

Finally, other EU impact assessments on similar legislative initiatives have assessed possible economic benefits from the proposed regulations. The impact assessment for the EU Non-financial Reporting Directive reports that surveyed companies listed as most important benefits: improvements related to credibility, overall transparency, risk management and the internal culture. It concludes that the regulation is expected to provide benefits for companies at the internal (i.e. better employee relations, improved management systems and internal processes, etc.) as well as external level (i.e. enhanced reputation, better perception by and dialogue with stakeholders, easier access to capital). The impact assessment also stipulates expected overall economic benefits from better management of risks and allocation of capital, enhanced trust in business and better resources management. The EU impact assessment on the Conflict Minerals Regulation indicates that the main benefits for companies are expected from "unquantifiable externalities which can be used for marketing purposes such as public image, Corporate Social Responsibility (CSR) and consumer satisfaction".

For the EU Timber Regulation[1181] (EUTR) the official Impact Assessment and the related background analysis as well as the latest biennial implementation report (2015-2017)[1182] and its related background analysis[1183] were reviewed.

According to the background report of the Impact Assessment[1184], the reduction of imports of illegal timber is expected to lead to a moderate increase in the price and production of timber and wood products in the EU. Especially forest owners would benefit as the value added in forestry is projected to increase 5-8 percent. On average and for all options (except option 2) the value added in the EU forest sector is expected to

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[1179] KPMG (2011) KPMG International Survey of Corporate responsibility Reporting 2011. Available at: https://assets.kpmg/content/dam/kpmg/pdf/2012/02/Corporate-responsiblity-reporting-2012-eng.pdf
[1180] Ernst & Young (2016). The state of sustainable supply chains - Building responsible and resilient supply chains. Available at https://www.ey.com/Publication/vwLUAssets/EY-building-responsible-and-resilient-supply-chains/$FILE/EY-building-responsible-and-resilient-supply-chains.pdf
[1181] See: https://ec.europa.eu/environment/forests/eutr_report.htm
[1182] European Commission (2018). Evaluation of Regulation (EU) No 995/2010 of the European Parliament and of the Council of 20 October 2010 laying down the obligations of operators who place timber and timber products on the market (the EU Timber Regulation). Retrieved from: https://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1538746572677&uri=COM:2018:668:FIN.
[1183] European Commission (2018). Background analysis of the 2015-2017 national biennial reports on the implementation of the European Union's Timber Regulation (Regulation EU No 995/2010). Retrieved from: https://ec.europa.eu/environment/forests/pdf/WCMC%20EUTR%20analysis%202017.pdf. Note: The biennial implementation report basically summarises the findings from the background analysis. There are also "national reports" available on the website, but these contain only the reporting forms for each MS which they had to fill out. All results from these reporting sheets are provided also in overview tables in the background analysis report and in a shortened form in the implementation report.
[1184] Indufor (2008). *Assessment of the impact of potential further measures to prevent the importation or placing on the market of illegally harvested timber or products derived from such timber*. Final Report. [online] Helsinki, Finland: Indufor in association with European Forest Institute (EFI). Available at: https://ec.europa.eu/environment/forests/pdf/ia_report.pdf [Accessed 10 Sep. 2019].

increase slightly more than 1 percent. The biennial implementation report discusses the implementation of the Regulation by Member States and does not discuss economic benefits.

The EU Impact Assessment on a proposed EU Regulation on Sustainable Investment (2018)[1185] describes two main regulatory options: Option 2 provides for a clarification of existing EU rules on duties towards investors/beneficiaries (non-legislative approach). Option 3 requires the integration of ESG factors in the investment process and the advisors' recommendation process as part of duties towards investors/beneficiaries (light regulatory approach).

The Impact Assessment focuses on general economic impacts rather than firm-specific impacts and describes the following expected overall economic impacts (pp. 105):

- By increasing the overall transparency, the different initiatives will reduce the asymmetry of information between end-investors, financial intermediaries and index provider.
- This enhanced transparency from the whole investment value chain will increase the reliability and attractiveness of ESG financial products and foster innovation in investment strategies and the design of these financial products.
- The proposed initiatives would also reduce the current market fragmentation in terms of methodologies for identifying environmentally sustainable activities/investments and developing low carbon benchmarks
- By fostering the development of more ESG products, the initiative would increase competition between financial intermediaries and therefore reinforce the efficiency of the market of ESG products.
- It would incentivise financial entities to be more innovative and to adopt higher ESG standards. This would ultimately increase the competitiveness of the European sustainable finance market.

In addition, the Impact Assessment foresees for both options (2 and 3) reputational benefits from increased disclosure on ESG integration and the higher comparability of disclosed ESG information, which could possibly attract new investors.

The EU Directive on the protection of the environment through criminal law, called Environmental Crime Directive (ECD) (Directive 2008/99/EC), lays down a list of environmental offences that must be considered criminal offences by all Member States.

The Impact Assessment[1186] for this Directive describes possible impacts of Policy Option 3 on business relatively generally as follows:

- It cites an OECD report which argues that companies which improved their environmental performance experienced a greater net probability of earning positive profits between 3-34%.

[1185] European Commission (2018). COMMISSION STAFF WORKING DOCUMENT IMPACT ASSESSMENT. Accompanying the document Proposal for a Regulation of the European Parliament and of the Council on the establishment of a framework to facilitate sustainable investment and Proposal for a Regulation of the European Parliament and of the Council on disclosures relating to sustainable investments and sustainability risks and amending Directive (EU) 2016/2341 and Proposal for a Regulation of the European Parliament and of the Council amending Regulation (EU) 2016/1011 on low carbon benchmarks and positive carbon impact benchmarks. Available at: https://eur-lex.europa.eu/legal-content/EN/ALL/?uri=CELEX:52018SC0265

[1186] European Commission (2007). COMMISSION STAFF WORKING DOCUMENT Accompanying document to the Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on the protection of the environment through criminal law IMPACT ASSESSMENT. Retrieved from: https://ec.europa.eu/smart-regulation/impact/ia_carried_out/docs/ia_2007/sec_2007_0160_en.pdf.

- Eliminating the illegal options on the market will encourage more investments in legal businesses.
- It will balance the competition between companies because businesses that respect often have already made significant investments to be able to comply with the strict existing rules are protected by tougher sanctions for their competitors who gain an unfair advantage by not complying.
- It will also improve the confidence of third countries businesses in the quality of products from the EU.

A review was carried out by EFFACE (European Union Action to Fight Environmental Crime), a 40-month EU funded research project. The objective was to assess the impacts of environmental crime as well as effective and feasible policy options for combating it from an interdisciplinary perspective, with a focus on the EU. The project ended in March 2016.The final synthesis[1187] report concluded that one of the main challenges was data and information management in the area of environmental crime. It does not assess economic impacts or benefits for firms.

No official impact assessment was found online on the EU Environmental Liability Directive (ELD, Directive 2004/35/EC), only a report on the implementation of the ELD, but economic benefits to firms are not discussed.[1188] The REFIT Evaluation only states that "it is difficult to quantify the benefits gained through prevention, in particular due to the lack of complete information on the total of preventive actions and other precautionary measures taken under the ELD".

The Seveso III Directive (2012/18/EU)[1189] aims at the prevention of major accidents involving dangerous substances as well as at limiting the consequences of such accidents for human health and the environment. The Directive requires operators to fulfil several obligations, including, for example, producing external emergency plans for high-risk establishments, and deploying land-use planning for the siting of establishments, making relevant information publicly available.

The Impact Assessment[1190] of the Seveso III Directive discusses mainly costs for operators, but also considers some benefits. As expected benefits the Impact Assessment describes the following:

- Improved emergency preparedness will mitigate the effects of major accidents and the costs of major accidents are avoided (as an example, it has been estimated that the Buncefield accident in England, in 2005, cost in the region of £1bn14).

[1187] European Union Action to Fight Environmental Crime (2016). ENVIRONMENTAL CRIME AND THE EU - Synthesis of the Research Project "European Union Action to Fight Environmental Crime" (EFFACE). Retrieved from: https://efface.eu/final-efface-report-environmental-crime-and-eu

[1188] Brussels, 14.4.2016 COM(2016) 204 final REPORT FROM THE COMMISSION TO THE COUNCIL AND THE EUROPEAN PARLIAMENT Report from the Commission to the Council and the European Parliament under Article 18(2) of Directive 2004/35/EC on environmental liability with regard to the prevention and remedying of environmental damage. Retrieved from: https://ec.europa.eu/transparency/regdoc/rep/1/2016/EN/1-2016-204-EN-F1-1.PDF. And COMMISSION STAFF WORKING DOCUMENT REFIT Evaluation of the Environmental Liability Directive Accompanying the document Report from the Commission to the European Parliament and to the Council pursuant to Article 18(2) of Directive 2004/35/EC on environmental liability with regard to the prevention and remedying of environmental damage. SWD/2016/0121 final. Retrieved from: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=SWD:2016:121:FIN

[1189] For more information, please see: European Commission (2019). Major accident hazards. Available at: https://ec.europa.eu/environment/seveso/legislation.htm.

[1190] See European Commission (2010). COMMISSION STAFF WORKING PAPER IMPACT ASSESSMENT Accompanying document to the Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on the control of major-accident hazards involving dangerous substances. Retrieved from: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52010SC1590.

- Improved business performance and competitiveness are expected as a result of better safety management systems which will increase efficiency and processes.

The benefits described for the different policy options are very specific to each option, e.g. they refer to reduced costs for operators which will not have to manage the provision of information to the general public (Option 5).

The latest Commission report available on the website, i.e. the Report on the Application in the Member States of Directive 96/82/EC on the control of major-accident hazards involving dangerous substances for the period 2009-2011, does not provide any information on the economic benefits for companies.

Based on the findings of these studies as well as the categorization of benefits in a recent study by the OECD (2016) on the costs, risks and benefits of due diligence for responsible business conducts, the main reports found in this literature review are grouped into the following categories of economic company-level benefits:

a) Financial and stock performance
b) Cost of capital
c) Brand image and reputation
d) Human resources
e) Risk management
f) Operational efficiency and innovation

It has to be kept in mind, however, that not all studies clearly distinguish between these categories as these are to some extent interrelated. For example, a good image and reputation, good risk management or operational efficiency, which are seen as results of sustainability and CSR measures, can be reflected in better financial performance measures in terms of stock market prices or accounting-based measurements like return on assets (ROA). As a result, the existing literature is discussed in these categories as far as possible, although it does not always fall exclusively into one category.

- **Financial and Stock Performance**

Extensive research has been carried out on the impact of sustainability measures conducted by companies on their financial or stock performance. Companies' activities related to sustainability and CSR can improve their financial and stock performance in different ways, many of which are discussed in more detail in other parts of this literature review. For example, on the income side, sustainability measures can increase a company's competitiveness or reputation and as a result promote its sales, leading to higher revenues, or improve its stock market performance. On the cost side, sustainability activities can help to save costs by increasing operational efficiency and cutting down resource costs or lead to lower capital cost due to reduced business risks. Financial performance has different dimensions and can thus be measured in different ways. Two main approaches to measuring financial performance are accounting indicators like ROA and stock performance as an indicator of the expected future performance of a company.

There has been an extensive realm of research over the past three decades on the relationship between the corporate social responsibility activities of companies and their financial performance. These include many academic works as well as industry studies and consulting reports. Most studies refer to ESG activities as sustainability indicators and find a slightly positive relationship between companies' activities and their financial performance, although findings are mixed.

One of the main meta-analyses (Margolis et al., 2009) assesses about 250 empirical studies from a period of about 35 years. The authors come to the conclusion that corporate social performance has an overall positive effect on corporate financial performance, but the effect is rather small. In addition, it suggests that revealed misbehaviour has a more pronounced effect on the financial performance of a company than doing well. Similarly, Fatemi et al. find that strong environmental, social, and governance performance increases a company's value and that weaknesses decrease it.[1191]

Another recent meta-analysis by Bassen et al. about the financial effects of environmental, social, and governance (ESG) criteria assesses about 2200 individual studies. The authors argue that the results of their meta-analysis show that the business case for ESG investing is empirically very well founded. Accordingly, the large majority of studies finds a positive relationship between environmental, social, and governance criteria and corporate financial performance, and this positive impact appears stable over time. In addition, almost all (90%) studies find a nonnegative relationship between ESG criteria and financial performance.[1192]

Eccles et al. based on statistical data of 180 companies suggest that companies which have been employing environmental and social policies in the past perform significantly better than a comparator group regarding stock market and accounting performance. The study also concludes that the effect is stronger in sectors where companies deal with consumers (B2C) not companies (B2B), where companies compete based on brands and reputations and where products depend on large amounts of natural resources.[1193]

Ameer et al. assess whether the top 100 sustainable global companies from the developed countries and emerging markets show a higher financial performance than a comparator group in 2008. The study concludes that in some sectors these companies indeed show higher (mean) sales growth, return on assets, profit, and cash flows from operations.[1194]

There are also some studies concluding that empirically no direct impact can be measured due to the broad scope and comprehensiveness of the used concepts or that the relationship between sustainability activities and financial performance may be bi-directional, i.e. it is not clear if good financial performance drives sustainability engagement or vice versa.

A second set of studies assesses the relationship between companies' sustainability activities and their stock market price performance. The reviewed studies are mainly of academic nature.

[1191] Fatemi, A. and Glaum, M. and Kaiser, S. (2017). ESG performance and firm value: The moderating role of disclosure. Global Finance Journal, Volume 38, 2018, Pages 45-64. Available at https://www.sciencedirect.com/science/article/pii/S1044028316300680

[1192] Bassen, A. and Busch, T. and Friede, G. (2015). ESG and financial performance: aggregated evidence from more than 2000 empirical studies, Journal of Sustainable Finance & Investment, 5:4, 210-233, DOI: 10.1080/20430795.2015.1118917

[1193] Eccles, R. G., and Ioannou, I. and Serafeim, G. (2014). "The Impact of Corporate Sustainability on Organizational Processes and Performance," Management Science, vol 60(11), pages 2835-2857. Retreived from: www.nber.org/papers/w17950

[1194] Ameer, R. and Othman, R. (2012). Sustainability Practices and Corporate Financial Performance: A Study Based on the Top Global Corporations. Journal of Business Ethics, June 2012, Volume 108, Issue 1, pp 61–79. Available at https://link.springer.com/article/10.1007/s10551-011-1063-y

A large meta-analysis by Clark et al. assesses the relationship between sustainable management in terms of environmental, social, and governance (ESG) issues and a company's economic performance. The meta-study is based on more than 200 different sources (academic articles, industry reports, news articles, books), covering 11 years from 2005 to 2015. The study finds a positive correlation between the sustainability business practices and the economic performance of companies. Based on 41 studies on the relationship between sustainability measures and financial market performance, the study finds that 80% of the assessed studies conclude that a company's stock price performance is positively influenced by its good sustainability practices.[1195]

The study by Eccles et al. tracks the stock market performance of the assessed 180 companies for two groups, the high- and low-sustainability companies, from 1993 to 2010. The results show that high-sustainability companies clearly outperform low-sustainability companies on the stock market[1196]: Investing 1 USD in assets in a value-weighted portfolio in the beginning of 1993, the investment would have grown by the end of 2010 to 22.6 USD for high-sustainability companies and only to 15.4 USD for the control companies (p. 20). Overall, stocks of high-sustainability companies outperform low-sustainability companies annually by 4.8%.[1197]

A study from 2018 revises 55 studies for the years 2010 to 2018. It finds that those studies that are linking CSR activities to company value indicate that higher CSR activities can lead to higher corporate value, higher equity returns and lower risk, enhancing the general collateral value of the company.[1198]

A major challenge is to find reports which do not merely assess whether a positive relationship exists, but a study which provides estimates about potential magnitudes. The only study which provides some numerical estimates in this regard is a project report by Bliss et al. (2015) which assesses the relationship between the corporate environmental, social, and governance practices and companies' financial, competitive, and wider business performance. The report, for that purpose, analyses over 300 existing studies (academic articles and other studies) complemented by interviews of executives and CR practitioners. It finds that corporate responsibility practices can increase the financial returns on investment as well as trigger related business and competitive benefits. It found that the potential impacts of corporate responsibility activities for different aspects of financial and stock performances are (p. 3):

- Over a 15-year period, increase shareholder value by (measure stated in the study: 1.28 billion USD)
- Increased valuation for companies with strong stakeholder relationships: 40-80%
- Reduced share price volatility: 2-10%
- Avoid market losses from crises: 378 million USD
- For a detailed list of the assessed studies, please see Annexure D, Table 1.

[1195] Clark, Gordon L. and Feiner, Andreas and Viehs, Michael (2015). From the Stockholder to the Stakeholder: How Sustainability Can Drive Financial Outperformance. Available at SSRN: https://ssrn.com/abstract=2508281 or http://dx.doi.org/10.2139/ssrn.2508281

[1196] The authors argue that due to the fact that companies are identified based on policy adoption decisions which were taken a sufficiently long time ago (which leads to a long time-lag between the independent and dependent variables), the likelihood of biases from reverse causality is mitigated.

[1197] Eccles, R. G., and Ioannou, I. and Serafeim, G. (2014). "The Impact of Corporate Sustainability on Organizational Processes and Performance," Management Science, vol 60(11), pages 2835-2857. Retreived from: www.nber.org/papers/w17950

[1198] Gerard, B. (2018). ESG and Socially Responsible Investment: A Critical Review. 2018. Social Science Research Network. Available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3309650

- **Cost of Capital**

The literature also suggests that sustainability activities of companies can have a positive impact on companies' economic and financial performance in regard to the cost of capital. Companies with good sustainability records may be more likely to attract investors (debt, equity, hybrid instruments) than other companies due to the expectation of reduced risks as discussed below. In addition, it is often argued that sustainability measures and related disclosure standards reduce information asymmetries between companies and investors. As a result, the cost of capital for such companies can be lower and access to capital can be eased.

A large amount of research, empirical assessments as well as literature reviews, has been conducted to assess the relationship between sustainability measures of companies and the cost of capital. These include general studies as well as country specific analyses and some studies focus on particular aspects such as environmental performance. The large majority finds that increase sustainability performance of companies is positively related to the cost of capital, i.e. increased sustainability performance causes lower costs of capital.

One of the major meta-analyses found is the study conducted by Clark et al., which assesses the relationship between sustainable management (environmental, social, and governance issues) and a company's economic performance. The study looked at different aspects of economic performance, one being the cost of capital. In this regard, it finds that 90% of the studies on the cost of capital indicate that good ESG standards lower the cost of capital for companies.[1199]

Another large meta-analysis based on 58 articles on the relationship between sustainability performance and/or sustainability disclosure and the cost of capital published between 2008 and 2018, comes to a similar conclusion. Despite some variance in the empirical results, it finds that most of the assessed studies find a statistically significant negative (in terms of correlation between the time series) relationship between the two variables. The authors conclude that these results suggest that the sustainability performance of a company is relevant for its value and that the valuation effect is also seen in the lower cost of capital for these companies.[1200]

As outlined above, Bliss et al. provide a literature review on the relationship between corporate environmental, social, and governance practices and financial performance. Based on their evaluations, they stipulate (as the only study) a quantitative estimate for cost reduction for equity of 1%.[1201]

Kölbel and Busch review various studies to assess the differences in results of two different types of studies, i.e. the analyses that are assessing the impact of sustainability measures on financial performance and the studies assessing the link of such measures

[1199] Clark, Gordon L. and Feiner, Andreas and Viehs, Michael (2015). From the Stockholder to the Stakeholder: How Sustainability Can Drive Financial Outperformance. Available at SSRN: https://ssrn.com/abstract=2508281 or http://dx.doi.org/10.2139/ssrn.2508281 NOTE 40

[1200] Gianfrate, G. and Schoenmaker, D. and Wasama, S. (2018). Cost of capital and sustainability: a literature review. Working paper series 03, Erasmus Platform for Sustainable Value Creation, Rotterdam School of Management. Available at https://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=5&cad=rja&uact=8&ved=2ahUKEwjdhZSr3vjhAhVEIVAKHTj8AiwQFjAEegQIBBAC&url=https%3A%2F%2Fwww.rsm.nl%2Ffileadmin%2FImages_NEW%2FErasmus_Platform_for_Sustainable_Value_Creation%2F11_04_Cost_of_Capital.pdf&usg=AOvVaw1Csckr51QrS7OOrmnzFYrH.

[1201] Bliss, R. and Jordan, S. and Rochlin, S. and Yaffe Kiser, C. (2015). Project ROI Report: Defining the Competitive and Financial Advantages of Corporate Responsibility and Sustainability. IO Sustainability, Lewis Institute for Social Innovation at Babson College. Available at https://www.issuelab.org/resource/project-roi-report-defining-the-competitive-and-financial-advantages-of-corporate-responsibility-and-sustainability.html with the cost of capital. They conclude that these different types of studies use different approaches with different inherent assumptions.[1202] This leads, on the one hand, to mixed results on the relationship between ESG criteria and financial performance, while, on the other hand, the link between ESG performance and the cost of capital is well established. They conclude that these results are due to a common explanation, i.e. that ESG performance is priced efficiently in financial markets. According to the authors, this explains why the high ESG performance has a neutral effect on investment performance, while it leads to lower capital costs.

Based on empirical data for US companies for the years 1992 to 2007, El Ghoul et al. assess how companies' CSR scores affect their cost of capital. The authors find that companies with socially responsible practices have significantly lower cost of equity capital. They also assess which CSR activities contribute particularly to reducing companies' cost of equity and find that investment in improving responsible employee relations, environmental policies, and product strategies are substantial contributors, while CSR activities related to community relations, diversity, and human rights are not.[1203]

Based on a sample of 3,000 companies over 23 years (1990-2013), Ng and Rezaee assess empirically the question whether and how different environmental, social, and governance dimensions as well as components of economic sustainability disclosure affect the cost of equity for companies. They find a negative relationship between corporate sustainability performance and the cost of equity capital, i.e. if sustainability performance increases, the cost of capital decreases.[1204] In addition, their findings suggest that only the environmental and governance sustainability performance dimensions contribute to this relationship.

La Rosa et al. assess the impact of corporate social performance on the cost of capital and access to it and find that if corporate social performance increases, the interest rate, i.e. the cost, for debt capital goes down. The assessment is based on a sample of listed non-financial European companies for the years 2005 to 2012.[1205]

Similarly, Cooper and Uzun assess, based on a large sample of U.S. firms across all industries from 2006 to 2013, the relationship between corporate social responsibility (ESG performance9 and the cost of debt financing. The authors find that companies with strong CSR have a lower cost of debt, especially companies in the manufacturing and financial industries. For their assessment they use four broad measures of CSR performance and two measures of the cost of debt. [1206]

For a detailed list of the assessed studies, please see Annexure D, Table 2.

[1202] Kölbel, J. and Busch, T. (2017). The link between ESG, alpha, and the cost of capital: Implications for investors and CFOs. corporate finance biz. 3/4. 82 - 85. Available at https://www.researchgate.net/publication/315815434_The_link_between_ESG_alpha_and_the_cost_of_capital_Implications_for_investors_and_CFOs

[1203] El Ghoul, S. and Guedhami, O. and Kwok, C. and Mishra, D. (2011). Does corporate social responsibility affect the cost of capital? Journal of Banking & Finance, 35, issue 9, p. 2388-2406. Available at https://EconPapers.repec.org/RePEc:eee:jbfina:v:35:y:2011:i:9:p:2388-2406

[1204] Ng, A. C. and Rezaee, Z. (2015). Business Sustainability Performance and Cost of Equity Capital. Available at: http://dx.doi.org/10.2139/ssrn.3148611

[1205] La Rosa, F., Liberatore, G., Mazzi, F. and Terzani, S. (2017). The impact of corporate social performance on the cost of debt and access to debt financing for listed European non-financial firms. European Management Journal, Volume 36, Issue 4, August 2018, Pages 519-529. Retrieved from: https://www.sciencedirect.com/science/article/pii/S0263237317301317

[1206] Cooper, E. and Uzun, H. (2015). Corporate Social Responsibility and the Cost of Debt. Journal of Accounting and Finance Vol. 15(8) 2015. Available at: https://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=1&cad=rja&uact=8&ved=2ahUKEwj5zu6lq-fkAhVC16QKHY6nC6gQFjAAegQIARAC&url=http%3A%2F%2Ft.www.na-businesspress.com%2FJAF%2FCooperEW_Web15_8_.pdf&usg=AOvVaw3XNr_z_aphBEidxEXc0bUR

- **Brand Image and Reputation**

Central perceived benefits of CSR and sustainability activities for a company are improved reputation and brand image. It is argued that CSR and sustainability activities not only lead to higher sales, but also enable a company to attract employees (discussed below in section D). Several studies have assessed the relationship between CSR activities and a company's reputation and tried to analyse whether these have brought any economic benefits to companies in the form of increased sales or better prices.

The studies usually assess different aspects of sustainability and most are based on surveys or experimental studies. The studies seem to find a positive impact, but it has to be kept in mind that many studies are survey-based, i.e. their results reflect consumer intentions rather than concrete purchase decisions.

An online survey conducted regularly by Nielsen among 30,000 consumers, shows that most consumers (55%) say they are willing to pay extra for products and services from companies that are committed to positive social and environmental impact. An additional assessment of sales data show that after one year the sales of products with sustainability claims on the packaging rose on average by 2% and the sales of products which promoted sustainability actions through marketing programs rose by 5%. The sales of products without sustainability claims or marketing shows a sales rise of only 1%.[1207]

Hainmueller and Hiscox carried out two large-scale experiments in 419 retail stores and 155 outlet stores in the United States to assess the impact of environmental certifications and product labelling on purchasing decisions. They find that the assessed environmental label had a substantial positive effect on sales among female customers, increasing sales by 8%. In contrast, there was no positive effect found for male customers.[1208]

Ferreira et al. assess if corporate social responsibility activities would positively influence consumer perception about the benefit and the value of the product, the judgment of fairness in the price differential charged for it, and the consumer's buying intention. The findings indicated that consumers perceived greater benefit and value in the product of the socially responsible company. As a result, consumers showed to be willing to pay 10% more for such products and perceived this price differential as being fair.[1209]

Choi and Ng use experimental methods to assess whether environmental and economic dimensions of sustainability have an effect on consumer responses. The authors find that economic and environmental sustainability information has a positive impact on the evaluation of a company and consumers' purchase intent.[1210] Similarly, Boccia et al. find, based on a choice experiment, a positive relationship between socially responsible initiatives of companies and attitudes of consumers towards them and their products. However, they also point out that corporate social responsibility is for most people not

[1207] Nielsen (2014). Doing Well By Doing Good. Available at https://www.nielsen.com/us/en/insights/reports/2014/doing-well-by-doing-good.html
[1208] Hainmueller, J. and Hiscox, M. (2015). Buying Green? Field Experimental Tests of Consumer Support for Environmentalism. Working Paper. Available at https://scholar.harvard.edu/hiscox/publications/buying-green-field-experimental-tests-consumer-support-environmentalism
[1209] Ferreira, D. A. and Avila,M.G. and Dias de Faria, M. (2010). Corporate social responsibility and consumers' perception of price. Social Responsibility Journal, Vol. 6 Issue: 2, pp.208-221. Available at https://doi.org/10.1108/17471111011051720
[1210] Choi, S. and Ng, A. (2011). Environmental and Economic Dimensions of Sustainability and Price Effects on Consumer Responses. Journal of Business Ethics, Volume 104, Issue 2, pp 269–282. Available at https://doi.org/10.1007/s10551-011-0908-8

the choice criterion for purpose, because traditional purchasing criteria, like the price, are more important.[1211]

Kimeldorf et al. highlight that in polls people often indicate that they would pay more for products which are manufactured responsibly by taking into account workers and environmental rights. However, the authors also point out that when consumers go shopping, they either forget these opinions or choose not to act on them. Nevertheless, the results of an experiment on the purchase of socks produced under good working conditions, which were labelled accordingly, indicate that even people with "modest means and education" choose for "conscious consumption".[1212]

Another recent study by Juergens and Erdmann (2019)[1213] aims to provide (based on a literature review, survey and interviews) qualitative background information on the role, importance and use of non-financial reporting (and its regulation) and ESG and carbon and climate data. The study concludes that "Reputational risk is seen as number one driver (73%) of the demand for ESG information". The authors also describe as other drivers for the provision of ESG information – i.e. also the expected advantages or benefits from the reporting of ESG information – demand by institutional and private clients (investors), a broader societal trend towards environmental awareness.

For a detailed list of the assessed studies, please see Annexure D, Table 3.

- **Human Resources**

Another potential benefit that can result for companies from their sustainability measures and CSR activities is a positive impact on their human resources as such measures can increase the loyalty and motivation of employees, leading to higher efficiency and productivity as well as better recruitment perspectives and lower staff turnover.

An online survey conducted regularly by Nielsen among 30,000 consumers in 60 countries found that 67% of respondents prefer to work for socially responsible companies.[1214]

Similarly, an often-quoted experimental study by Greening and Turban[1215] finds that prospective job applicants are more likely to pursue jobs from socially responsible companies than from companies with poor social performance reputations. The authors conclude that a company's corporate social performance may influence especially high-quality candidates to choose one company over another and therefore lead to a competitive advantage by attracting and retaining high-quality candidates.

A large survey among 1,726 university students on their goals, job criteria and job satisfaction found that more than a third of the future employees would take a 15% pay

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[1211] Boccia, F, Malgeri Manzo, R, Covino, D. (2019). Consumer behavior and corporate social responsibility: An evaluation by a choice experiment. *Corp Soc Resp Env Ma*. 2019; 26: 97– 105. Available at https://doi.org/10.1002/csr.1661
[1212] Kimeldorf, Howard, Rachel Meyer, Monica Prasad, and Ian Robinson. "consumers with a conscience: will they pay more?." contexts 5, no. 1 (2006): 24-29. Available at: https://journals.sagepub.com/doi/pdf/10.1525/ctx.2006.5.1.24
[1213] DIW, Berlin. Juergens, I. and Erdmann, K. (2019). A short qualitative exploration of the reporting and use of non-financial data in the context of the fitness check of the EU framework for public reporting by companies. DIW Berlin.
[1214] Nielsen (2014). Doing Well By Doing Good. Available at https://www.nielsen.com/us/en/insights/reports/2014/doing-well-by-doing-good.html
[1215] Greening, D. W., and Turban, D. B. (2000). Corporate Social Performance as a Competitive Advantage in Attracting a Quality Workforce. *Business & Society*, *39*(3), 254–280. https://doi.org/10.1177/000765030003900302.

cut to work for a company committed to social responsibility and nearly one-half (45%) would do so for a job that makes a social or environmental impact.[1216]

Similarly, the meta-analysis by Clark et al. assesses the relationship between sustainable management and a company's economic performance.[1217] In this context the study argues, based on findings by Edmans that good reputation regarding the working conditions can increase the company's attractiveness for employers and can help to retain workers.[1218]

Vitaliano assesses company's voluntary turnover (quit) rates. This study finds that measures leading to a rating as a socially responsible company correlate with a reduction of the annual quit rate by 3-3.5%, which amounts to a 25-30% reduction compared to companies which are not ranked as socially responsible.[1219]

The same study by Juergens and Erdmann[1220] mentioned above concludes that, apart from the main driver of the demand for ESG information being reputational risk, this demand for information on such sustainability information is also driven by the competition for talent.

For a detailed list of the assessed studies, please see Annexure D, Table 4.

- **Risk Management**

Most supply chains today are international and include many different suppliers and stakeholders in different regions. Due diligence is understood as a comprehensive risk management process to identify, assess, prevent and mitigate the risks within these complex supply chains. Research indicates, on the one hand, that sustainability measures can reduce business risks, and, on the other hand, this reduced risk can result in a concrete economic impact for companies.

Sassen et al. assess the impact of corporate social performance (operationalised by environmental, social, and governance factors) on market-based company risk in Europe. The authors find that better corporate social performance - especially in the social dimension - can increase company value through lower company risk.[1221]

Kumar et al. study the link between ESG and risk to assess if stock prices of ESG positive companies perform better than stocks from non-ESG companies. The study finds that companies, which incorporate ESG factors show lower volatility in their stock performances than the comparator group in the same industry. They also find that each

[1216] Szeltner, M. and Zukin, C. (2012). Talent Report: What Workers Want in 2012. Study by Net Impact and Rutgers University. Available at https://www.netimpact.org/research-and-publications/talent-report-what-workers-want-in-2012
[1217] Clark, Gordon L. and Feiner, Andreas and Viehs, Michael (2015). From the Stockholder to the Stakeholder: How Sustainability Can Drive Financial Outperformance. Available at SSRN: https://ssrn.com/abstract=2508281 or http://dx.doi.org/10.2139/ssrn.2508281 NOTE 40
[1218] Edmans, A. (2012). The Link Between Job Satisfaction and Firm Value, with Implications for Corporate Social Responsibility. Academy of Management Perspectives 26(4), 1-19, November 2012. Available at SSRN: https://ssrn.com/abstract=2054066 or http://dx.doi.org/10.2139/ssrn.2054066
[1219] Vitaliano, D. F. (2010). Corporate social responsibility and labour turnover. Corporate Governance: The international journal of business in society, Vol. 10 Issue: 5, pp.563-573. Available at https://doi.org/10.1108/14720701011085544
[1220] DIW, Berlin. Juergens, I. and Erdmann, K. (2019). A short qualitative exploration of the reporting and use of non-financial data in the context of the fitness check of the EU framework for public reporting by companies. DIW Berlin.
[1221] Sassen, R.; Hinze, A.K.; Hardeck, I. (2016). Impact of ESG factors on firm risk in Europe. Journal of Business Economics, Volume 86, Issue 8, pp 867–904. Available at https://link.springer.com/article/10.1007%2Fs11573-016-0819-3

industry is affected differently by ESG factors, and that ESG companies generate higher returns.[1222]

Eccles et al. also find that the portfolio of high sustainability companies experiences lower volatility (1.43% and 1.72% on a value-weighted and equal-weighted base) than the portfolio of low sustainability companies (1.72% and 1.79%, respectively).[1223]

McKinsey interviewed leaders from sustainable companies in 2014. The interviews suggest that the economic value that can be at stake from sustainability issues can reach up to 70% of a company's earnings (before interest, taxes, depreciation, and amortisation). It shows that effective risk management can have a substantial economic impact for a company. The study reports that business leaders pursue sustainability matters because they believe it has a material financial impact. The economic value considered to be at stake from risks related to reputation (e.g. reputational damage based on perceived misuse of resources) is estimated at 70% of a company's earnings, while the value at stake from risks related to rising operation costs (e.g. increasing raw-material costs due to increased demand/lower supply) is estimated at 60% and the value at stake from risks related to possible supply chain disruptions is 25% (e.g. production delay or cancellation due to lack of access).[1224]

For a detailed list of the assessed studies, please see Annexure D, Table 5.

- **Operational Efficiency and Innovation**

Some authors argue that sustainability measures can have an impact on a company's operational efficiency and innovation. Accordingly, sustainability measures can lead to a more efficient use of resources and therefore result in cost-savings for a company. Similarly, it is suggested that a focus on sustainability and resource efficiency can provide opportunities for innovations in the form of new products (e.g. green products) or new process and logistics solutions. However, these relationships are mainly discussed in relation to case studies of selected companies.

According to the meta-analysis conducted by Clark et al., most studies show a positive relationship between sustainability and operational performance. In fact, 88% of the studies show that solid ESG practices result in better operational performance. This is particularly the case for environmental measures (e.g. corporate environmental practices, pollution abatement, and resource efficiency). The authors argue that empirical research clearly indicates that good corporate environmental practices positively influence the competitiveness of companies and therefore lead to better corporate performance. Regarding social factors, employee relationship and good workforce practices are found to have a large impact on operational performance. However, the authors also point out that there is a lack of research on the direct link

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[1222] Kumar, N.C.A. and Smith, C. and Badis, L. and Wang,N. and Ambrosy, P. and Tavares, R. (2016). ESG factors and risk-adjusted performance: a new quantitative model. Journal of Sustainable Finance & Investment. Available at http://dx.doi.org/10.1080/20430795.2016.1234909

[1223] Eccles, R. G., and Ioannou, I. and Serafeim, G. (2014). "The Impact of Corporate Sustainability on Organizational Processes and Performance," Management Science, vol 60(11), pages 2835-2857. Retreived from: www.nber.org/papers/w17950

[1224] McKinsey (2017) Sustainability's deepening imprint. Available at: https://www.mckinsey.com/business-functions/sustainability/our-insights/sustainabilitys-deepening-imprint#

between other types of corporate social measures such as worker-safety standards in emerging markets and respect for human rights.[1225]

Eccles and Serafeim also argue that including ESG issues in their sustainability framework leads to cost savings for companies through innovation, resource efficiency, and revenue enhancements due to sustainable products.[1226]

McKinsey found evidence that increased efficiency in the use of resources is an indicator of better financial performance. They found a significant correlation between resource efficiency of companies within a sector and their financial performance. Those companies that performed best in each sector were also those which had the most ambitious sustainability strategies.[1227]

Whelan and Fink provide several examples of companies which have benefitted economically from resource and process efficiencies due to their sustainability programs. For example, they cite the company Dow which has invested 2 billion USD since 1994 in improving resource efficiency but in return has saved 9.8 billion USD from reduced energy, waste and water consumption. Another example is Wal-Mart, which increased its fleet efficiency and saved almost 11 million USD due to improved fuel efficiency.[1228]

In a 2012 report on sustainability for consumer business companies Deloitte concludes that sustainability is recognised increasingly as a primary driver for strategic product and business model innovation. The report argues that truly innovative companies have put sustainability at the heart of their business examining strategic decisions based on the criterion of sustainability.[1229]

For a detailed list of the assessed studies, please see Annexure D, Table 6.

1.1.3 Impact on Company-Level Competitiveness

According the European Commission's Better Regulation Policy,[1230] the EU is determined 'to ensure that its proposals meet policy goals at minimum cost and deliver maximum benefits to citizens, businesses and workers while avoiding all unnecessary regulatory burdens. This is key to support growth and job creation – allowing the EU to ensure its competitiveness in the global economy - while maintaining social and environmental sustainability.' These objectives need to be taken into consideration for the assessment of the potential impact of due diligence policies on company-level competitiveness.

The literature on the impact of due diligence regulations on company-level competitiveness points to two broader types of implications: the impact on cost competitiveness and the impact on other factors that may impact on a company's overall competitiveness in its respective markets, including its sourcing markets. The cost

[1225] Clark, Gordon L. and Feiner, Andreas and Viehs, Michael (2015). From the Stockholder to the Stakeholder: How Sustainability Can Drive Financial Outperformance. Available at SSRN: https://ssrn.com/abstract=2508281 or http://dx.doi.org/10.2139/ssrn.2508281 NOTE 40
[1226] Eccles, R. G., and Serafeim, G. (2013). The performance frontier: Innovating for a sustainable strategy. Harvard Business Review, May 2013, 50-60. Available at https://hbr.org/2013/05/the-performance-frontier-innovating-for-a-sustainable-strategy
[1227] McKinsey (2017) Sustainability's deepening imprint. Available at: https://www.mckinsey.com/business-functions/sustainability/our-insights/sustainabilitys-deepening-imprint#
[1228] Whelan, T. and Fink, C. (2016). The Comprehensive Business Case for Sustainability. Harvard Business Review. Available at https://hbr.org/2016/10/the-comprehensive-business-case-for-sustainability.
[1229] Deloitte (2012). Sustainability for consumer business companies. A story of growth. Available at https://www2.deloitte.com/hr/en/pages/consumer-business/articles/sustainability-for-consumer-business-companies.html
[1230] European Commission (2019). Better regulation in the European Commission. Available at https://ec.europa.eu/info/sites/info/files/better-regulation-guidelines-better-regulation-commission.pdf

competitiveness impact is mainly a function of the 1) administrative burden and 2) transparency-induced decreases on companies' refinancing costs (see also Cost of Capital). The second group of factors comprises competitive advantages, e.g. advantages in attracting and retaining employees, greater consumer loyalty, less operational delays, less problematic relations with governments and local communities, and less reputational risks and damages.

It is generally difficult to quantify changes in companies' relative competitiveness. While a quantification of the cost impact is generally feasible on the basis of industry data and survey results, the impact of other factors on changes in the competitive position of a company is difficult to quantify without having access to detailed company-level data (corporate due diligence). As a result, it is methodologically difficult to weigh the pecuniary competitive disadvantages against the benefits.

It should be noted though that several recent studies highlight that globalisation of business and investment activities has increased the demand for more transparent accounting of corporate responsibilities encompassing human rights, social, economic and environmental dimensions. Consequently, the relative competitive advantage of proactive companies that engage in CSR activities over other companies might have increased over time. However, as pointed out by Loikkanen and Hyytinen, for example, the relationship between CSR measures and competitiveness vary among different companies due to varying sectoral characteristics, including geography of markets and production, company size, role in business and value and supplier chains. Thus, the CSR impact on competitiveness may actually need to be examined in detail by each company separately to arrive at meaningful conclusions.[1231]

Table 8.3: The impact of due diligence regulations on companies' competitiveness

Study	Impact on Competitiveness
National Association of Manufacturers (2011) on Section 1502 of US Dodd-Frank Act	• Stress that the application of the rules only to reporting companies would unfairly affect them relative to non-reporting companies and damage their competitive position • Also refer to the market for auditing services and potential scarcity of specified auditing services, which may result in higher compliance costs for companies affected by the policy
Bayer and de Buhr (2011) on Section 1502 of US Dodd-Frank Act	• Do not directly address the impact on companies' relative competitiveness, but make a few remarks about efficiency • Refer to joint industry initiatives, e.g. the creation of common platforms for information collection, tracking, reporting and auditing, to reduce the labour effort/cost burden on companies, which would reduce the negative impact on companies' relative loss in competitiveness
IPC (2011) on Section 1502 of US Dodd-Frank Act	• State that Compliance with the proposed rules will impose a significant burden on all subject companies and their suppliers • Argue that non US issuers will remain outside the SEC's (the policy scope's) jurisdiction and therefore enjoy a significant competitive advantage over US companies that do file reports

[1231] Loikkanen and Hyytinen (2011). Corporate Social Responsibility and Competitiveness – Empirical Results and Future Challenges. Chapter in book Environmental Management Accounting and Supply Chain Management (pp.151-170).

	with the SEC
European Commission (2013) on Non-financial Reporting requirements	• Authors argue that a strategic approach to CSR can bring benefits in terms of risk management, cost savings, access to capital, customer relationships, human resource management and innovation capacity • Highlight a number of factors that can be relevant to a company's overall business success and competitiveness respectively: lower cost of capital in terms of debt (loans and bonds) and equity, competitive advantage in attracting, motivating and retaining talented employees, consumer loyalty • Argued that failure to adequately manage relationships with stakeholders can result in operational delays, higher costs of insurance and security, problematic relations with governments and local communities, and potential reputational damages • Distinguish between efficiency and competitiveness, whereby efficiency relates to the implications for the administrative burden resulting from compliance with the proposed policies. Point out that some of the proposed measures would increase companies 'external competitive factors,' while compliance costs would generally increase, which negatively impact on forms cost competitiveness • Voluntary measures (option 2c in the analysis) are stated to be neutral with respect to the impact on compliance costs • With respect to the consultation conducted by the authors, it is stated that none of those established in EU Member States where more stringent mandatory disclosure requirements are already enforced reported any competitiveness problems compared to those established in Member States with less stringent legislation • It is outlined that EU companies would indeed have to bear slightly higher costs than companies established or headquartered in third jurisdictions where non-financial disclosure is not regulated, i.e. EU companies' global competitiveness would decrease • Overall, it is stated that the additional administrative burden would be fairly limited, and that the potential benefits are likely to outweigh the cost, i.e. EU companies relatively more competitive on a global level
Loikkanen and Hyytinen (2011)	• Highlight that link between CSR measures and competitiveness varies for different companies due to a great number of varying sectoral characteristics

1.1.4 Impact on SMEs

From an economic perspective, market regulations are often reported as a barrier to market entry and an external factor decreasing companies' competitiveness due to the administrative costs that result from compliance requirements. For SMEs, regulations are generally perceived as a hurdle to company-level growth although they are, as indicated by a recent meta-study, not necessarily identified as a hurdle in principal.[1232] The reduction of red tape and bureaucracy is broadly welcomed as beneficial for SME growth. At the same time, the literature on property rights and corruption, for example, suggests that regulation is necessary to create a sense of stability and security as instability and uncertainty can generally inhibit companies' growth ambitions.

The European Commission explicitly recognises the specific needs of SMEs. The Small Business Act (SBA), an overarching framework for the EU policy on SMEs, generally aims to simplify the regulatory and policy environment for SMEs.[1233] The Commission's regulatory fitness and performance (REFIT) programme, which is part of the EU's better regulation agenda, paying particular attention to SMEs, aims to ensure that EU legislation delivers results for small businesses effectively, efficiently and at minimum cost.[1234] A 2014 public consultation on the SBA found that administrative and legislative burden is the top concern for EU SMEs (SBA 2014).

The literature on the impact of due diligence regulations on SMEs indicates that SME businesses can be directly and indirectly affected by such policies (see Table 8.4). Many studies distinguish between the impacts on SMEs that directly fall under the scope of the regulations, e.g. publicly-listed SMEs in the case of the EU's Non-financial reporting Directive, and SMEs that are affected by second round effects, e.g. small companies that have to report relevant information to corporate customers or suppliers that are directly affected by the regulation, as in the case of the EU and US conflict minerals policies.

The major findings for company-level effects of due diligence and reporting requirements for SMEs can be summarised as follows:

1) The relative administrative burden of SMEs (per unit cost of compliance) is generally greater than for larger companies,
2) SMEs may have a competitive disadvantage vis-à-vis larger companies due to a lack of human resources,
3) SMEs may suffer from tighter contractual obligations imposed by their large corporate clients,
4) SMEs may not have the sufficient leverage to extract the necessary information from their supply chain partners, especially if their supply chain extends to foreign countries.

One study highlights the regulatory challenge to mandate principles of transparency and accountability in the value chains without driving SMEs out of business. The latter notion is considered important by the authors of this assessment of options as far-reaching (broad in scope) human rights due diligence regulations may trigger costly second round effects for SMEs.

However, it should also be noted that some of the literature relates reporting and disclosure requirements, which may arguably operate disproportionately for SMEs who

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[1232] Beis (2018). Understanding the firm-level effects of regulations in the growth of small- and medium-sized enterprises. BEIS Research Paper Number 10.
[1233] European Commission (2019). The small business act for Europe. Available at https://ec.europa.eu/growth/smes/business-friendly-environment/small-business-act_en.
[1234] European Commission (2019). REFIT – making EU law simpler and less costly. Available at https://ec.europa.eu/info/law/law-making-process/evaluating-and-improving-existing-laws/refit-making-eu-law-simpler-and-less-costly_en.

are effectively required to produce statements similar in length and detail to larger companies. In this way, such studies may have limited relevance to due diligence requirements as a standard of expected conduct, which requires a proportionate response to existing risk.

Table 8.4: The impact of due diligence regulations on SMEs

Study	Impact on SMEs
National Association of Manufacturers (2011) on Section 1502 of US Dodd-Frank Act	Impact on SMEs[1235]: • State that many SME manufacturers who are not subject to SEC reporting will be affected by the regulation. • State that SMEs will face larger per unit cost increases because of smaller business volumes, more limited resources to produce the required documentation, and less leverage over their suppliers, both foreign and domestic. • State the SMEs have a relative disadvantage as they lack compliance staff. • Argue that SMEs may be pushed out of the market, which may result in a shrinking the supplier base.
Bayer and de Buhr (2011) on Section 1502 of US Dodd-Frank Act	• Highlight the challenge to mandate principles of transparency and accountability in the value chains without excessively burdening the private sector actors and driving smaller enterprises out of business. • Consider companies with annual revenues of 100 million USD as the threshold value between small and large companies.
IPC (2011) on Section 1502 of US Dodd-Frank Act	• State that mandatory due diligence would impose significant burdens especially those companies that are small businesses. • Argue that the proposed rules would present an extensive burden to small and large companies, particularly in the initial years following implementation. • Point out that larger companies will likely impose contractual requirements on the small companies regardless of SEC exemptions for small companies. • Argue that smaller companies may not have the leverage needed to extract the necessary information from their supply chain, especially if that supply chain extends outside the United States.
European Commission (2014) on Conflict Minerals	• Distinguish between companies with less and more than 250 employees. • Lower absolute initial cost burden found for SMEs. • Lower absolute recurrent cost burden found for SMEs.
European Commission (2013) on Non-financial Reporting requirements	• Argue that large companies and business associations expressed concerns that stricter mandatory disclosure requirements could be excessively burdensome, in particular for SMEs, and undermine efforts that the industry is already taking on a voluntary basis and negatively affect competitiveness. • State that publicly listed SMEs are already required to produce corporate governance statements. • Argue that the impact on non-listed SMEs limited. • State that for non-listed companies, best corporate governance

[1235] Kimpel, S. (2011). Memorandum on the Conflict Minerals Regulation. File No. S7-40-10. Available at https://www.sec.gov/comments/s7-40-10/s74010-212.pdf

	practices of SMEs can be encouraged on voluntary basis.

1.1.5 Industry and Aggregate Economic Impacts

Impact assessments of CSR and due diligence policies are mainly based on company-specific case studies. At the same time, various studies are available for specific sectors of the economy. However, data on the net economic impact, e.g. the impact after weighing companies' costs against the commercial benefits companies may gain are rarely available. Existing studies generally conclude with a number of qualitative assessments/statements about the impacts of certain CSR or due diligence policies.

RIMAS, for example, in 2011 conducted an analysis of CSR practices for the automotive industry. The study concludes that car manufacturers are actively engaging in CSR practices as they face environmental and health concerns and have to account for changes in the regulatory environment. In addition, the authors state that customers increasingly pose demands with respect to safety, comfort, and fuel efficiency in terms of better cost/quality. As a result, car makers increasingly have to compete in terms of both prices and corporate practices aiming to meet various societal goals. The authors did, however, not conduct a quantitative cost-benefit analysis.[1236]

Mazur-Wierzbicka argues that European agricultural companies can apply CSR measures to gain additional economic, social and environmental benefits without, however, providing estimates for the size of these effects.[1237]

Martinuzzi et al. study how CSR policies can impact on the European textiles sector. They argue that for industrial textiles manufacturers CSR shows some similarities to chemical industry. CSR might be a driver of product quality, with positive feedback effects on sales, and may reduce the environmental impact of production procedures. The authors argue that CSR measures may therefore result in competitive advantage for the industry, but they do not provide estimates for the costs and benefits.[1238]

It should be noted that the commercial impact of CSR and due diligence requirements varies from company to company. This has generally been confirmed by the economic impact assessments available for the EU's Non-financial Reporting Directive and the conflict minerals policies imposed by the EU and the US. To the knowledge of the authors of this report, comprehensive economic impact assessments that quantitatively weight the aggregate costs against the aggregate benefits are neither available on a sector nor an economy-wide basis. However, some impact assessment provide aggregate numbers for the overall cost impact (one-off costs and recurrent costs) to be borne by those companies that are directly and indirectly affected by the regulations (see Annexure D, Table 6 on total first-year costs and Table 7 on total recurrent costs).

1.2 Social Impacts

A large body of literature on CSR practices, usually case studies, focuses on a rather broad range of issues related to social impacts, e.g. education, public health, community

[1236] RIMAS (2011). CSR Activities and Impacts of the Automotive Sector. Working Paper No. 03/2011. Available at https://www.sustainability.eu/pdf/csr/impact/IMPACT_Sector_Profile_AUTOMOTIVE.pdf
[1237] Mazur-Wierzbicka (2015). The Application of Corporate Social Responsibility in European Agriculture. Regional Studies on Development, 19, 1, 2015. Department of Human Resource Management Faculty of Economics and Management University of Szczecin.
[1238] Martinuzzi, A., Kudlak, R., Faber, C. and Wiman, A. (2011). CSR Activities and Impacts of the Textile Sector. Research Institute for Managing Sustainability (RIMAS) Vienna University of Economics and Business.

welfare, entrepreneurship development, environment, commercial marketplace development and rural development. These areas of the societal impacts of corporate activities are usually not related to the core business functions of companies. With the exception of large, publicly-listed companies, businesses' activities in these areas are generally not required by law and usually pursued on a voluntary basis.

The 2015 UN Global Compact bulletin outlines individuals and groups whose rights might be impacted (positively and negatively) through a company's operations and business relationships. They distinguish between a company's own employees and third-party employees such as supply chain workers, contract workers and other business partners' employees. It is also highlighted that people living in communities around production facilities might be affected by companies' operations, while others might be indirectly affected by companies' environmental footprint.[1239]

Women, indigenous people, elderly persons, persons with disabilities, children as well as religious or ethical minorities are considered groups that are likely to face higher risks regarding potentially harmful practices and impacts. According to an assessment of the UN Global Compact (2016), problems associated with adverse social impact include, for example, insufficient grievance mechanisms for affected groups, inadequate working conditions for contract workers and casual labourers, excessive working hours, discrimination against trade unions, unequal opportunities regarding hiring and promoting women, adverse impacts of tourism activities on the local population (on their environment, privacy, food security and traditional way of life etc.). The adverse impacts of corporate activity on human rights and the environment are well-documented in various studies and databases like the Business and Human Rights Resource Centre.

The OECD summarises that for workplace conditions, elements of 'responsible business practices' include, for example, the respectful treatment of employees in matters related to recruitment and selection, diversity and equal opportunity, work/life balance, professional development and progression, and full entitlement to employment rights.[1240]

As concerns company-level impacts on companies who adopted and reported on CSR activities, numerous studies confirm positive effects of CSR policies on a company's labour force. CSR activities can generally have a positive effect on human resources, and they can increase the loyalty and motivation of employees, leading, for example, to higher efficiency and productivity as well as better recruitment perspectives and lower staff turnover rates.[1241]

For existing impact assessments, it should be noted that social impacts are generally discussed in a qualitative way. Accordingly, impact assessments only indicate the general direction of impact, but mostly do not provide numerical estimations. In addition, available impact assessments do not provide sensitivity analyses, e.g. how social impacts vary for different industries and jurisdictions.

The impact assessments on non-financial reporting requirements and due diligence obligations largely focus on the potential impact on workers and working conditions. Thereby a wide range of impacts on workers and employment conditions is covered, e.g.

[1239] UN Global Compact Bulletin (2015). Available at: https://www.unglobalcompact.org/library/3051

[1240] OECD (2016). Quantifying the Costs, Benefits and Risks of Due Diligence for Responsible Business Conduct Framework and Assessment Tool for Companies- June 2016. Available at https://mneguidelines.oecd.org/Quantifying-the-Cost-Benefits-Risks-of-Due-Diligence-for-RBC.pdf

[1241] See Nielsen (2014); Szeltner, M. and Zukin, C. (2012); Clark, Gordon L. and Feiner, Andreas and Viehs, Michael (2015).

working conditions such as working hours, wages and salaries, discriminatory practices related to gender, age, and nationality, and the representation of workers in companies' decision-making bodies (see Table 8.5). However, the impacts on other rights-holders who are not workers are less well-documented.

In the EU's impact assessment on the EU Conflict Minerals Regulations, survey respondents share mixed expectations regarding various social impacts (beyond just the impact on workers) resulting from the proposed policies. About half of the respondents do not expect social impacts resulting from the conflict minerals due diligence procedures. The impact on workers and working conditions has not been addressed in detail. Those who expected negative impacts mention that the regulations may contribute to impoverishment and unemployment, embargos and losses in general economic activity. Those respondents who expected positive impacts indicate that the regulations may have a positive impact on political and social stability in the affected regions, which might be conducive to economic activity.

In the EU's impact assessment on the EU Non-financial Reporting Directive, the social impact is mainly assessed for recruitment practices and the impact on affected companies' employees, while some information is given for aggregate employment effects. It is argued that non-financial disclosure and reporting requirements would contribute to more diversified boards and enhance equality of treatment and opportunities for different groups of people (gender, age, nationality, background, etc.). It is also stated that reporting obligations may result in more flexible corporate policies regarding work life and family life. The authors also highlight that increased transparency on employment-related matters could contribute to support better employment relations and contribute to lower risks and costs associated with labour conflicts. Regarding the impact on overall employment, it is stated that the proposed policies could contribute in a limited extent to the creation of jobs in the field of CSR (without an assessment of where these effects take place). Negative impacts on employment, which could result from the higher costs of reporting, are considered negligible due to the limited administrative burden of the proposed policies.

Table 8.5: Potential social impacts resulting from disclosure and due diligence regulations

Study	Potential social impacts
European Commission (2014) on Conflict Minerals	• According to survey results, 55% of the respondent do not expect a social impact of conflict minerals due diligence procedures (neither positive nor negative). • According to survey results, 45% of the respondent do expect a social impact of conflict minerals due diligence procedures (positive nor negative). • As regards positive impacts, it is argued that conflict minerals due diligence will have a positive impact on political and social stability in the regions 60%), increase international awareness of the underlying problems (27%), improve the environment (7%) and contribute to the defunding of warlords (6%). • As concerns negative impacts, it is argued that conflict minerals due diligence will contribute to impoverishment and unemployment (22%), embargos and losses in economic activity (18%), increased bureaucracy (18%), more corruption (16%) and an increase in violence (5%), while 21% of the respondent did not anticipate

	'further negative effects'.
European Commission (2013) on Non-financial Reporting requirements	• Social impact is primarily assessed for recruitment practices and impact on affected companies' employees, while some information is given for aggregate employment effects. • It is argued that non-financial disclosure and reporting requirements would contribute to more diversified boards and enhance equality of treatment and opportunities for different groups of people (gender, age, nationality, background, etc.). • It is argued that the policies may have an indirect impact on the reconciliation between private/family and professional life, e.g. more women in key positions and more flexible policies regarding work life and family life. • It is found that affected companies would be encouraged to better identify potential risks relating to human rights, including labour rights. • It is found that increased transparency on employees- and human capital matters could contribute to support better employment relations and contribute to lower risks and costs associated with labour conflicts. • As concerns the impact on overall employment, it is stated that the proposed policies could contribute in a limited extent to the creation of jobs in the field of CSR, while negative impacts on employment, which could result from the higher costs of reporting, are considered negligible due to the limited administrative burden of the proposed policies.

The EU Impact Assessment on the Timber Regulation[1242] (for a more detailed description of the EUTR, please see Table 1.2) assesses social impacts mainly regarding employment effects in the forest industry. These employment effects seem to be deducted from the estimated impacts on production resulting from the partial equilibrium modelling. The method for calculating employment effects is the assumption that "a reduction in production volume is coupled with a proportionate decline in employment".[1243] This is projected to lead to a change in employment in forest industries as follows for:

- Option 1 (Expansion of the FLEGT VPA approach): Projected to result in reduction production of forest industries and employment in exporting countries to the EU of -2.4% to 0.5% for 2009-2015 and -15.7% to 2.4% for 2016 – 2020. In the EU, the changes in all regions are projected to be quite limited.
- Option 3 (Border measures to prevent the importation of illegally harvested timber): Projected to result in reduction production of forest industries and employment in exporting countries to the EU of -0.4% to 0.3% for 2009-2015 and -0.8% to 0.4% for 2016 – 2020. In the EU, the border measures (option 3) have almost no impact on the employment in forest industries.
- Option 4A (Legislation which prohibits the trading and possession of timber and timber products harvested in breach of the laws of the country of origin) & 4B

1242 See COMMISSION STAFF WORKING DOCUMENT Accompanying document to the Proposal for a Regulation of the European Parliament and the Council determining the obligations of operators who make timber and timber products available on the Market. IMPACT ASSESSMENT Report on additional options to combat illegal logging. Available at: https://ec.europa.eu/environment/forests/pdf/impact_assessment.pdf

1243 Indufor et al. (2008). Assessment of the Impact of Potential Further Measures to Prevent the Importation or Placing on the Market of Illegally Harvested Timber or Products Derived from Such Timber, Final Report. Retrieved from: https://ec.europa.eu/environment/forests/pdf/ia_report.pdf.

(Legislation which requires that only legally harvested timber and timber products be placed on the market): The impact on employment is projected to be modest. The reason is that changes in production volume of forest industries are expected to be very limited. Similarly, to the impact of border measures, the changes in EU employment are very small.

Other social aspects are considered to depend on the extent to which social provisions have been incorporated in the definition of legality. Social aspects relating to equal opportunities, private life and access to social welfare systems are considered to not be affected and are not discussed.

The Impact Assessment[1244] of the Seveso III Directive does not discuss impacts on employment or other social impacts except for stating that impacts will vary or that there is no significant impact expected.

No official impact assessment was found online on the EU Environmental Liability Directive (ELD, Directive 2004/35/EC), only a report on the implementation of the ELD[1245] which does not assess any social or employment impacts. Similarly, the Impact Assessment[1246] on the EU Directive on the protection of the environment through criminal law (Directive 2008/99/EC) does not assess any social or employment impacts. An evaluation of the latter is ongoing, but there are no public results yet, the draft report is expected for November.[1247]

1.3 Impacts on Human Rights

According to the UN Guiding Principles Reporting Framework, human rights due diligence is: "An ongoing risk management process… in order to identify, prevent, mitigate and account for how [a company] addresses its adverse human rights impacts. It includes four key steps: assessing actual and potential human rights impacts; integrating and acting on the findings; tracking responses; and communicating about how impacts are addressed."

While the sections above focused on impacts of due diligence frameworks and practices at the company level, this section will flip the conversation and focus on due diligence impacts for rights-holders. There are various kinds of due diligence practices with varying effects on the ability of governments to meet their human rights obligations and perform their duties, and for holders to demand their rights. To stay in line with the purposes of this study, this section reviews the relevant literature on the impacts for rights-holders from three different kinds of due diligence practices: 1) Voluntary due diligence practices and guidelines; 2) Reporting requirements; and 3) Mandatory due

[1244] See European Commission (2010). COMMISSION STAFF WORKING PAPER IMPACT ASSESSMENT Accompanying document to the Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on the control of major-accident hazards involving dangerous substances. Retrieved from: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52010SC1590.

[1245] Brussels, 14.4.2016 COM(2016) 204 final REPORT FROM THE COMMISSION TO THE COUNCIL AND THE EUROPEAN PARLIAMENT Report from the Commission to the Council and the European Parliament under Article 18(2) of Directive 2004/35/EC on environmental liability with regard to the prevention and remedying of environmental damage. Retrieved from: https://ec.europa.eu/transparency/regdoc/rep/1/2016/EN/1-2016-204-EN-F1-1.PDF.
And COMMISSION STAFF WORKING DOCUMENT REFIT Evaluation of the Environmental Liability Directive Accompanying the document Report from the Commission to the European Parliament and to the Council pursuant to Article 18(2) of Directive 2004/35/EC on environmental liability with regard to the prevention and remedying of environmental damage. SWD/2016/0121 final. Retrieved from: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=SWD:2016:121:FIN

[1246] European Commission (2007). COMMISSION STAFF WORKING DOCUMENT Accompanying document to the Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on the protection of the environment through criminal law IMPACT ASSESSMENT. Retrieved from: https://ec.europa.eu/smart-regulation/impact/ia_carried_out/docs/ia_2007/sec_2007_0160_en.pdf.

[1247] See: https://ec.europa.eu/info/law/better-regulation/initiatives/ares-2018-4981980_en diligence. While the literature on the implementation of due diligence requirements at the company level is vast, the conversation around the actual impacts of due diligence practices on specific human rights is limited.

Recognising this drawback, this section commences by reviewing the existing impact assessments carried out prior to the implementation of relevant EU regulations as well as implementation assessments after the implementation. Thereafter, this section reviews the existing literature outlining positive impacts of the various forms of due diligence, and finally concludes with a review of literature investigating respective challenges.

1.3.1 Pre-Implementation Impact Assessment Review

The table below summarises human rights impacts found in impact assessments carried out prior to the implementation of relevant EU regulations. A common feature across these evaluations is that the quantification of the effects on human rights are difficult to trace. Positive human rights effects are often derived indirectly from changes in companies' conducts due to reputational concerns.

The table begins by analysing the EU Commission Impact Assessment on Additional Options to Combat Illegal Logging. There is a well-acknowledged link between corruption, organized crime, and the illegal exploitation of natural resources, including forests. In certain countries where logging resources are plenty, profits are such that they institutionalize corruption, undermine the rule of law, risk violent conflict, and disregard respect for human rights. EU policy regarding illegal logging was set out in the Forest Law Enforcement, Governance and Trade (FLEGT) Action Plan of which one of its key measures is a licensing scheme for the prevention of importing illegal logging into the EU. The scheme would be implemented as part of the Voluntary Partnership Agreements (VPAs). While the VPA approach was considered to be promising, it was understood that it may have limitations. The EU FLEGT Action Plan therefore assessed five additional measures including 1) expansion of the FLEGT VPA approach; 2) Further development of voluntary measures by the private sector; 3) Border measures to prevent the importation of illegally harvested timber; 4A) Legislation which prohibits the trading and possession of timber and timber products harvested in breach of the laws of the country of origin; 4B) Legislation which requires that only legally harvested timber and timber products be placed on the market. While Option 4B touches on the risk of accepting legality certificates from countries which might be in violation of serious human rights abuses—and thus providing them with illegitimate credibility—the Impact Assessment did not explicitly assess impacts for rights holders.

The table below follows by reviewing the EU Commission Impact Assessment of EU NFRD Proposal[1248]. The EU NFRD was proposed in the frame that disclosure requirements had not yet covered aspects of significance for rights holders, specifically regarding human rights and corruption. Those that did disclose human rights aspects, included isolated and anecdotal information. A key motivation for the EU NFRD proposal was the longstanding recognition of transparency issues in holding companies accountable to

[1248] Non-financial Reporting Directive (2014). Directive 2014/95/EU of the European Parliament and the Council of 22 October 2014 amending Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups. Available at https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014L0095&from=DE

respect their duties and responsibilities towards rights holders. Moreover, existing non-financial reports often focus on less controversial issues and avoid discussion of any negative human rights impacts. The Impact Assessment reviewed five possible policy options including 1) voluntary annual statements; 2) mandatory detailed, stand-alone non-financial reporting; 3) non-financial report on a "report or explain" basis; 4) voluntary reporting; 5) mandatory EU standard. The assessment's preferred options, 1 and 2a, are expected to have a beneficial impact on fundamental rights as they would encourage EU companies to regularly review their policies and internal procedures in various aspects, mainly due to a larger public scrutiny.

Thereafter the EU Assessment of Due Diligence Compliance Cost, Benefit and Related Effects on Selected Operators in Relation to the Responsible Sourcing of Selected Minerals[1249], outlines the impacts of six policy options. The need for updated policy options is founded on flaws within existing legislation such as the US DFA. According to the assessment, while the OECD Guidance does not, others due diligence mechanisms, such as the US DFA, are ambiguous about how to treat minerals in situations where security forces are not perpetrators of serious human rights abuses for which a risk management plan can be adopted. By engaging in mining and trading activities, companies are at risk of contributing to the financing of non-state armed groups which perpetuate conflict and the associated human rights abuses in conflict-affected and high-risk areas.

As such, the impact assessment investigates six policy options for regulating these activities including 1) Standalone EU Communication; 2) a "soft-law" approach; 3) Voluntary regulation establishing obligations under an "EU responsible importer" certification based on the OECD Guidance; 4) Mandatory regulation establishing obligations under an "EU responsible importer" certification based on the OECD Guidance; 5) a directive establishing obligations for EU-listed companies based on the OECD Guidance; and 6) an import ban when EU importers of ores fail to demonstrate compliance with the OECD Guidance. While the study does not explicitly assess human rights impacts, options 3, 4, and 6 touch on possible indirect effects. Specifically, indirect benefits based on reputation can be expected from Option 3 as a voluntary "EU responsible importer" certification based on the OECD Guidance would encourage demand for ethically and legitimately sourced minerals, leading to formalized mining sectors, more sustainable development and benefits for local communities. However, if such a certification becomes mandatory, such as in Option 4, the full reach of possible benefits may be put at risk as companies may seek the easiest, least risky and burdensome way of complying (avoiding sourcing from conflict-affected regions). This could trigger negative impacts on local communities as mineral flows could be diverted towards companies with lower standards and norms. Finally, the most effective of the policy options is expected to be Policy Option 6, implementing a prohibition of imports when EU importers of ores fail to demonstrate compliance with the OECD Guidance as this ban would have indirect positive effects through increased government interventions to ensure that due diligence is exercised.

[1249] See European Commission (2014), Impact Assessment Accompanying the document Proposal for a Regulation of the European Parliament and of the Council setting up a Union system for supply chain due diligence self-certification of responsible importers of tin, tantalum and tungsten, their ores, and gold originating in conflict-affected and high-risk areas. PART 1 (Impact Assessment). Available at: https://eur-lex.europa.eu/resource.html?uri=cellar:b05a9c8f-a54d-11e3-8438-01aa75ed71a1.0001.01/DOC_1&format=PDF

The EU Impact Assessment of Directive 2008/99/EC on the protection of the environment through criminal law, which lays down a list of environmental offences that must be considered criminal offences by all Member States if committed intentionally or with serious negligence, then reviews three policy options, with the first being no action at the EC level. The second policy option consists of encouragement for cooperation between Member States, and the third explored option regards minimum regulatory standards. While the Impact Assessment does not specifically discuss human rights impacts of Option 1 and 2, Option 3 does touch on indirect impacts. Option 3 is to set minimum regulatory standards, which are expected to increase human health as the harmonization of environmental offence definitions may facilitate targeting the most serious cases. This will likewise increase sanction levels and extend the scope of liability.

The Seveso Directives are the main EU legislation dealing specifically with the control of on-shore major accident hazards involving dangerous substances. The Seveso III Directive came into force on 1 June 2015, replacing the Seveso II Directive. The EU Impact Assessment of the Seveso III Directive investigates six possible policy options including the first aimed at the alignment of Annex I to classification, labelling, and packaging regulations (CLP) and the second policy option that builds on this to also include other technical amendments to Annex I. Policy issue three then proposes procedures for adapting Annex I in the future, policy issue four regards information to the public and information management systems including reporting, and policy option five discusses land-use planning. Finally, the sixth and final policy issue provides clarifications to facilitate effective implementation. Impacts on human rights under all possible options of the Seveso Directive depend on how many establishments will fall under the Directive, and how many will be newly included within the scope. Where there is a decrease in the number of establishments under the directive, this might lead to a decrease in human and environmental health protection. However, where there is an increase in scope, this would lead to an increase in protection. Specifically, under policy option 4 which establishes information access to the public and the establishment of information management systems including reporting, there would be positive impacts on protection levels for human health (both for workers and the public) and the environment.

Table 8.6. Impact Assessments carried out prior to the implementation of regulation with potential human rights impacts

Pre-implementation Impact Assessments	Human Rights Impacts
EU Commission Impact Assessment on Additional Options to Combat Illegal Logging (2008)[1250,1251]	
Baseline scenario	No discussion of human rights impacts.
Option 1 – Expansion of the FLEGT VPA approach	
Option 2 – Voluntary measures by the private sector further developed	
Option 3 – Border measures to prevent the importation of illegally harvested timber	
Option 4A – Legislation which prohibits the trading and possession of timber and timber products harvested in breach of the laws of the country of origin	
Option 4B – Legislation which requires that only legally harvested timber and timber products to be placed on the market	Option 4B applies the requirement for certification of legality to all market operations for timber products. The absence of an internationally agreed definition of legality and the issue of what would constitute a credible proof of it would represent a considerable challenge for the design of such an approach as there would be a risk of accepting "legality" documents from countries with serious credibility issues such as human rights abuses. This might indirectly negatively impact responsibility towards rights holders as those in violation might receive illegitimate credibility.
EU Commission Impact Assessment on EU NFRD Proposal (2013)[1252]	

1250 See COMMISSION STAFF WORKING DOCUMENT Accompanying document to the Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL determining the obligations of operators who make timber and timber products available on the Market. IMPACT ASSESSMENT Report on additional options to combat illegal logging. Available at: https://ec.europa.eu/environment/forests/pdf/impact_assessment.pdf

1251 Indufor (2008). Assessment of the impact of potential further measures to prevent the importation or placing on the market of illegally harvested timber or products derived from such timber. Final Report. [online] Helsinki, Finland: Indufor in association with European Forest Institute (EFI). Available at: https://ec.europa.eu/environment/forests/pdf/ia_report.pdf [Accessed 10 Sep. 2019].

1252 See COMMISSION STAFF WORKING DOCUMENT IMPACT ASSESSMENT Accompanying the document Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL amending Council Directives 78/660/EEC and 83/349/EEC as regards disclosure of non-financial and diversity information by certain large companies and groups. Available at https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52013SC0127

<table>
<tr><td>Option 0 – No policy change</td><td></td></tr>
<tr><td>Options 1 on an Annual Statement</td><td rowspan="2">The preferred options 1 and 2a are expected to have a beneficial impact on fundamental rights as they would encourage EU companies to regularly review their policies and internal procedures in various aspects, mainly due to a larger public scrutiny. In particular, the nonfinancial disclosure requirement is expected to have a positive impact on:

• the workers' right to information (Article 27 of the Charter of Fundamental Rights of the EU137)
• human rights awareness within companies
• reducing instances of EU company involvement in human rights infringements
• the right to non-discrimination (Article 21 of the EU Charter)
• Equality between women and men (Article 23).
• Freedom to choose an occupation and right to engage in work (Article 15)
• Freedom of expression and information (Article 11).
However, as the preferred policy options would not require processing of personal data, they not impact rights to privacy and data protection (Articles 7 and 8 of the EU Charter).</td></tr>
<tr><td>Option 2a Requiring a detailed, stand-alone non-financial report on a mandatory basis</td></tr>
<tr><td>Option 2b – Requiring a detailed non-financial report on a “report or explain” basis (companies are allowed to explain why they have not reported).</td><td rowspan="3">The report only provides a preliminary assessment of impacts for the preferred options: Option 1 and Option 2a.</td></tr>
<tr><td>Option 2c – Voluntary reporting</td></tr>
<tr><td>Option 3 – Setting up a mandatory EU standard</td></tr>
</table>

EU Conflict Minerals – Assessment of Due Diligence Compliance Cost, Benefit and Related Effects on Selected Operators in Relation to the Responsible Sourcing of Selected Minerals (2014)[1253]	
Option 1 – Standalone EU Communication and **Option 2** "Soft-law" approach	There is no specific discussion on human rights impacts.
Option 3 – Regulation establishing obligations under an "EU responsible importer" certification based on the OECD Guidance (Voluntary)	Indirect benefits based on reputation. This option would encourage demand for ethically and legitimately sourced minerals, leading to formalised mining sectors, more sustainable development and benefits for local communities.
Option 4 – Regulation establishing obligations under an "EU responsible importer" certification based on the OECD Guidance (Mandatory)	Companies may seek the easiest, least risky and burdensome way of complying (avoiding sourcing from conflict-affected regions). This could trigger negative impacts on local communities as mineral flows could be diverted towards companies with lower standards and norms.
Option 5 – Directive establishing obligations for EU-listed companies based on the OECD Guidance	Similar impacts to Option 4.
Option 6 – Prohibition of imports when EU importers of ores fail to demonstrate compliance with the OECD Guidance (Import ban)	Indirect positive effects through increased government interventions to ensure that due diligence is exercised.
EU Impact Assessment of Directive 2008/99/EC on the protection of the environment through criminal law[1254]	
Option 1 – No action on EC level	No specific discussion on human rights impacts.
Option 2 – Encourage cooperation between Member States	No specific discussion on human rights impacts.
Option 3 – Set minimum regulatory standards	No discussion on direct human rights impacts. However, possible indirect impacts include increase in human health as harmonization of environmental offence definitions may facilitate the targeting of most serious cases. This will

1253 See European Commission (2014), Impact Assessment Accompanying the document Proposal for a Regulation of the European Parliament and of the Council setting up a Union system for supply chain due diligence self-certification of responsible importers of tin, tantalum and tungsten, their ores, and gold originating in conflict-affected and high-risk areas. PART 1 (Impact Assessment). Available at: https://eur-lex.europa.eu/resource.html?uri=cellar:b05a9c8f-a54d-11e3-8438-01aa75ed71a1.0001.01/DOC_1&format=PDF

1254 See COMMISSION STAFF WORKING DOCUMENT Accompanying document to the Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on the protection of the environment through criminal law. IMPACT ASSESSMENT. Available at: https://ec.europa.eu/smart-regulation/impact/ia_carried_out/docs/ia_2007/sec_2007_0160_en.pdf

	likewise increase sanction levels, and extend the scope of liability.
EU Impact Assessment of Directive 2012/18/EU – Seveso III Directive[1255]	
Policy Issue 1 – Alignment of Annex I to CLP;	Impacts on human rights under all possible options of the Seveso Directive depend on how many establishments will fall under the Directive, and how many will be newly included within the scope. Where there is a decrease in the amount of establishments under the directive, this might lead to a decrease in human and environmental health protection. However, where there is an increase in scope, this would lead to an increase in protection.
Policy Issue 2 – Other technical amendments to Annex I;	
Policy Issue 3 – Procedures for adapting Annex I in the future	
Policy Issue 4 – Information to the public and information management systems including reporting	Specifically, under policy option 4 which establishes information access to the public and the establishment of information management systems including reporting, there would be positive impacts on protection levels for human health (both for workers and the public) and the environment.
National Regulations	
French Duty of Vigilance Law	No IA available.
Dutch Child Labour Due Diligence Law	
Italian Decree on Due Diligence	
Spanish Law on Environment and Human Rights	
Swiss Advanced Legislative Proposal	

[1255] See COMMISSION STAFF WORLING PAPER. IMPACT ASSESSMENT Accompanying document to the Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on the control of major-accident hazards involving dangerous substances. Available at: https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52010SC1590&from=EN

1.3.2 Post-Implementation Impact Assessment Review

Regarding post-implementation studies, the Table 8.7 presents the human rights-related conclusions of the Environmental Liability Directive (ELD) and the EU Timber Regulation. While both regulations are of greater relevance for the assessment of environmental impacts, both are worth a review for any links to impacts for rights holders. Furthermore, the ELD does not involve reporting or due diligence requirements, however, its evaluation provides relevant criteria to consider during the refinement and design of policy options, namely, coordination and harmonisation with existing guidelines and regulations, information availability, and the scope of different types of liability.

The European Commission's Report on the Implementation of the Environmental Liability Directive (2016), which establishes a framework based on the polluter pays principle to prevent and remedy environmental damage, demonstrates that a key added value of the ELD refers to the recognition of stakeholder's rights. According to both the Estonian and German Case Study Reports, up to date information on the notification of environmental damage or threat of it and the rights of the persons concerned can be found online. According to Articles 7(4) and 12 of the ELD, a person who could be affected by the damage, or with a legitimate interest, as well as environmental NGOs, have rights to request the implementation of prevention and remedial measures, by submitting the relevant information. The competent authority is obliged to evaluate the request and to notify the requestor of the decision.

EU Timber Regulation Implementation Reports are a series of biennial reports that synthesize the results of the national reports submitted by all 28 EU Member States providing a review of the implementation of the EU Timber Regulation (EUTR). The EUTR is the first legal mandatory due diligence instrument at the EU level. As mandatory due diligence is regarded as key for corporate sustainable responsibility under the UNGPs, the regulation is notable. In accordance with Article 20(1), of the regulation EU Member States and EEA/EFTA countries are required to submit a report on the implementation of their actions every other year. These reports act as important monitoring and evaluation tools as well as a way for stakeholders to share best practices. While the report does not directly discuss human rights implications, section 1.4 on environmental impacts will discuss the regulation in more depth.

Table 8.7. Post-implementation Impact Assessments

Post-Implementation Impact Assessments/Studies	Relevant findings
EU Directive 2004/35/EC – Environmental Liability Directive[1256,1257]	
The ELD aims to establish "a framework for the prevention and remedying of environmental damage through a liability based on the 'polluter-pays principle' in order to ensure that biodiversity is restored or maintained at Favourable Conservation Status, and thus halting biodiversity loss in the EU." It requires that "operators whose activity has caused biodiversity damage or imminent threat of such damage, to be held liable."	An added value of the ELD refers to the recognition of rights holders under the directive. According to Articles 7(4) and 12 of the ELD, a person who could be affected by the damage, or with a legitimate interest, as well as environmental NGOs, have rights to request the implementation of prevention and remedial measures. The competent authority is then obliged to evaluate the request and to notify the requestor of the decision.
EU Timber Regulation Implementation Reports[1258,1259]	
As indicated above, the EUTR have three key obligations: (1) The placing on the market of illegally harvested timber or timber products is prohibited; (2) Operators who are placing timber and timber products on the EU market for the first time are required to exercise due diligence (risk management); (3) Traders of timber and timber products already placed on the EU market are required to keep record of their suppliers and customers (obligation of traceability).	No discussion on human rights impacts.

1.3.3 Benefits and Challenges of the Different Policy Approaches

[1256] Milieu Ltd., IUCN (2014). Experience gained in the application of ELD biodiversity damage. Final report for the European Commission, DG Environment. [online] Brussels. Available at: https://ec.europa.eu/environment/legal/liability/pdf/Milieu%20report%20-%20ELD%20Biodiversity%20Damage.pdf [Accessed 11 Sep. 2019].
[1257] The report describes the implementation challenges of the ELD based on the analysis of 10 EU Member States environmental liability regimes. There are no pre-implementation impact assessments available for this regulation.
[1258] See COMMISSION STAFF WORKING DOCUMENT Evaluation of Regulation (EU) No 995/2010 of the European Parliament and of the Council of 20 October 2010 laying down the obligations of operators who place timber and timber products on the market (the EU Timber Regulation). Available at: https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52016SC0034&from=EN
[1259] See REPORT FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT AND THE COUNCIL Regulation (EU) No 995/2010 of the European Parliament and the Council of 20 October 2010 laying down the obligations of operators who place timber and timber products on the market (the EU Timber Regulation). Biennial report for the period March 2015 – February 2017. Available at: https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52018DC0668&from=EN

- **Voluntary Guidance on Due Diligence**

As previously reviewed in the preceding sections, there are various voluntary mechanisms for conducting human rights due diligence. The existing literature reviews successful case studies and areas for possible expansion to enhance positive implications of voluntary guidelines including the

1) UN Guiding Principles (UNGP);
2) OECD Due Diligence Guidance;
3) EU Conflict Minerals Regulation
4) Equator Principles;
5) IFC Performance Standards;
6) Voluntary Principles on Security and Human Rights (extractive sector);
7) International Council on Mining and Metals;
8) UNEP International Cyanide Management Code

The UN Guiding Principles on Business and Human Rights are probably the most central texts in framing due diligence standards, and the most referenced in the conversation of positive impacts. The principles are grounded on three key acknowledgments:

a) States' existing obligations to respect, protect and fulfil human rights and fundamental freedoms;
b) The role of business enterprises as specialized organs of society performing specialized functions, required to comply with all applicable laws and to respect human rights;
c) The need for rights and obligations to be matched to appropriate and effective remedies when breached.

According to the literature, one of the key achievements of the Guiding Principles has been to shift the approach to business and human rights from a retrospective liability for corporate violations to a proactive one designed to prevent adverse human rights impacts via due diligence. However, complications arise when identifying the responsible party as the principles fail to clearly allocate duties and distinguish the requirements of corporations from those of their third-party suppliers. As such, the literature proposes that the principles have demonstrated benefits for proactively protecting rights-holders, as long as corporations refrain from passing on the burden of due diligence down the supply chain.[1260] To avoid that this due diligence is passed along the supply chain, and in order to set coherence between the Guiding Principles and the framework for companies' actions, the responsibilities of business enterprises are defined in Guiding Principle 13. This Guiding Principle establishes that business enterprises have a responsibility to: avoid *causing or contributing* to adverse human rights impacts through their own activities; and seek to prevent or mitigate human rights impacts that are *directly linked* to their operations, products or services by their business relationships, even if they have not contributed to those impacts.[1261]

[1260] Jonathan Bonnitcha, Robert McCorquodale, The Concept of 'Due Diligence' in the UN Guiding Principles on Business and Human Rights, European Journal of International Law, Volume 28, Issue 3, August 2017, Pages 899–919. Retrieved from: https://doi.org/10.1093/ejil/chx042

[1261] UNHR Office of the High Commissioner. Guiding Principles on Business and Human Rights.(2011) Page 19. Accessed at https://www.ohchr.org/documents/publications/GuidingprinciplesBusinesshr_eN.pdf

Beyond the transition from a retrospective to a proactive approach to protecting right-holders, some authors have discussed potential additional benefits derived from the Ruggie and UNGP framework[1262]. For instance, Sanders[1263], has pointed out that 'corporate responsibility to respect' in the second pillar of the UN Guiding Principles represents a promising analogy with the tort of negligence in domestic jurisdictions for rights-holders to draw on. Developing the analogy in detail, Sanders concluded that the similarities are more significant than any differences. Similarly, Van Dam has highlighted the similarities between human rights due diligence and tort law principles across common law and civil law jurisdictions.[1264] Aftab has also highlighted the usefulness of the UNGPs due diligence standard as a legal standard of care.[1265]

However, despite these similarities with the legal standard of care, this study's country case studies show that there are very few examples of cases where the UNGPs or its due diligence expectations were successfully employed to demonstrate binding legal obligations.

[1262] UN Human Rights Council (2008). Promotion and protection of all human rights, civil, political, economic, social and cultural rights, including the right to development. Report of the Special Representative of the Secretary-General on the issue of human rights and transnational corporations and other business enterprises, John Ruggie. Available at: https://www.business-humanrights.org/sites/default/files/reports-and-materials/Ruggie-report-7-Apr-2008.pdf

[1263] Sanders, Astrid (2014). The Impact of the 'Ruggie Framework' and the United Nations Guiding Principles on Business and Human Rights on Transnational Human Rights Litigation. LSE Legal Studies Working Paper No. 18/2014. Available at: https://ssrn.com/abstract=2457983

[1264] Cees Van Dam 'Tort Law and Human Rights: Brothers in Arms – On the Role of Tort Law in the Area of Business and Human Rights' (2011) *JETL* 221.

[1265] Yousuf Aftab 'The Intersection of Law and Corporate Social Responsibility: Human Rights Strategy and Litigation Readiness for Extractive-Sector Companies," 60 *Rocky Mt. Min. L. Inst.* 19-1 (2014).

Table 8.8: Literature on Positive HR Impacts of Voluntary Due Diligence Approaches

Study	Key Findings	Regulatory Option	Relevant Regulation	Source
The Concept of Due Diligence in the UN Guiding Principles on Business and Human Rights	A key achievement of the Guiding Principles has been to shift the focus from retrospective to proactive. However, the UNGP are unclear distinguishing requirements among actors along the supply chain.	2	UNGP	Bonnitcha J., McCorquodale R., 2017
Human Rights Responsibilities in the Oil and Gas Sector: Applying the UN Guiding Principles	While much positive progress is already being made by many in the sector towards implementation of the Guiding Principles, work remains to be done and this article has identified some of the challenges and complexities the oil and gas sector continues to face in utilizing due diligence tools to achieve human rights mandates.	2	UNGP	Lindsay R., McCorquodale R., Blecher L., Bonnitcha J., Crockett A., Sheppard A., 2013
Tourism and water: from stakeholders to rights-holders, and what tourism businesses need to do	To comply with due diligence, companies need policies and procedures to undertake human rights impact assessments that they are currently lacking in Bali. This is an extension of environmental and social impact and risk assessments that many companies already routinely undertake. The business opportunities from undertaking human rights impact assessments were considered. If undertaken they can represent a significant potential business opportunity for companies to show their responsibility for respecting human rights, as well as for enhancing reputation, investor confidence, staff retention, production and profitability, as well as brand image.		n/a	Stroma C., 2014
Tort Law and Human Rights: Brothers in Arms On the Role of Tort Law in the Area of Business and Human Rights	Van Dam highlights similarities between human rights due diligence and tort law principles, particularly in what in concerns the use of tort law to prevent transnational corporations from being involved in human rights violations either directly or via their subsidiaries and suppliers. Van Dam clarifies that tort law looks at what a corporation ought to have known (and ignorance of it is not a defence against liability), therefore carrying out 'due diligence' for the corporation is not a choice but a duty.		n/a	Van Dam C., 2011

The Intersection of Law and Corporate Social Responsibility: Human Rights Strategy and Litigation Readiness for Extractive Sector Companies	The Guiding Principles are for Aftab a clear candidate to form the standard of care that would be of reference once a duty of care has been established. The principles could however not become the substantive basis of a claim, but as the principles become a widely accepted standard for human rights risk management, they can constitute a significant tool to prove corporate negligence when corporate actions are not up to these standards.		UNGP	Aftab Y., 2014
What Conflict Minerals Rules Tell us About the Legal Transplantation of CSR Standards without the State: From the UN to the US to Taiwan	This study investigates the effects of two forms of U.S. due diligence (voluntary and mandatory) on foreign host country governance. In regards to voluntary due diligence, the study finds that the Electronic Industry Citizenship Coalition (EICC)'s Code of Conduct has caused changes in company behaviour beyond US companies, but likewise Taiwanese company behaviour. The study argues this change may demonstrate that due diligence might have been transplanted into Taiwan through private channels such as supply contracts, rather than through state governance. The study likewise finds that companies shift behaviour more prominently in response to the EICC code in comparison to the Dodd Frank Act suggesting that bottom- up approaches may be more effective or more easily accepted than public standards such as state laws enacted by a foreign/national government in a top-down approach.		EICC Code of Conduct	Tsai & Wu, 2018
Dynamic Governance Interactions: Evolutionary Effects of State Responses to Non-State Certification Programs	This article examines how states have responded to the emergence of forest and fisheries certification programs, arguing that while structural management differences are of influence, state responses typically strengthen the non-state program.			Gulbrandsen, Lars H., 2014

Investments in Weak Governance Zones	While the summary of the 2005 consultations only touches on the ability of responsible multi-national company behaviour to contribute to state governance, it highlights opportunities. Specifically the consultations concluded that both guiding principles by international organisations as well as policies designed by home governments of companies investing in foreign territory can and do play a role in helping weak governance countries develop healthier institutions.			OECD, 2005

While literature focusing on positive impacts is scarce, a few studies spoke on opportunities for sector-specific due diligence to impact human rights regarding the right to water and occupational safety rights. For example, using Bali as a case study, Cole Stroma investigates the possibilities of due diligence in the tourism sector to impact the right to water and argues that there is an opportunity for companies to extend the currently required environmental impact assessment to include human rights impact assessments as well.[1266] Furthermore, in the context of the oil and gas sector, Lindsay et al. point out that while the Guiding Principles do not, of themselves, create new law, it is evident that corporate ignorance of human rights duties can have legal consequences for business enterprises operating in the oil and gas sectors (OGBEs) as a result of even voluntary due diligence mechanisms, hence making companies more aware of the need to respect human rights.[1267]

Regarding challenges, the literature is significantly more extensive in discussing challenges for the aforementioned schemes to have positive human rights impacts. While it has been established that the UNGPs make corporations more accountable to rights-holders, the effectiveness of human rights due diligence is still in many respects dependent on corporations' willingness to act. According to Fasterling and Demuijnck, this does not only represent a missed opportunity to increase the respect for human rights commitments, but it could also depreciate the fundamental norms that voluntary due diligence schemes aim to establish.[1268] An even more fundamental challenge is the fact that due diligence has not been homogenously defined across UN documents, making it harder to implement. McCorquodale and Bonnitcha point out that the UNGPs describe due diligence both as a ***process***[1269] that business should have in place to monitor and avoid human rights impacts[1270], and a standard of care similar to the legal standard of due diligence.[1271] In a 2009 report[1272] to the UN Human Rights Council, Ruggie[1273] described due diligence as a ***standard of conduct***[1274] that companies should meet to discharge their responsibility to respect human rights. In other words, the report states that companies should act with due diligence to avoid infringing on the rights of others.[1275]

[1266] Stroma Cole (2014) Tourism and water: from stakeholders to rights holders, and what tourism businesses need to do, Journal of Sustainable Tourism, 22:1, 89-106, DOI: 10.1080/09669582.2013.776062

[1267] Rae Lindsay, Robert McCorquodale, Lara Blecher, Jonathan Bonnitcha, Antony Crockett, Audley Sheppard, Human rights responsibilities in the oil and gas sector: applying the UN Guiding Principles, *The Journal of World Energy Law & Business*, Volume 6, Issue 1, March 2013, Pages 2–66, https://doi.org/10.1093/jwelb/jws033

[1268] Fasterling B., Demuijnck G. (2013). Human Rights in the Void? Due Diligence in the UN Guiding Principles on Business and Human Rights. Journal of Business Ethics. (Vol. 116, No. 4). Special Issue on Universal Ethics, Cultural Diversity and Globalization – 17th IESE International Symposium. Pp. 799 – 814. Springer.

[1269] Guiding Principle 17 states that business should carry out human rights due diligence and "The process should include assessing actual and potential human rights impacts, integrating and acting upon the findings, tracking responses, and communicating how impacts are addressed."

[1270] Framework, Report to the UN Human Rights Council (Business and Human Rights Report), UN Doc. A/HRC/11/13, 22 April 2009, paragraph 25. This definition is consistent with the Framework Report stating that: due diligence – a process whereby companies not only ensure compliance with national laws but also manage the risk of human rights harm with a view to avoiding it.'

[1271] Jonathan Bonnitcha, Robert McCorquodale, The Concept of 'Due Diligence' in the UN Guiding Principles on Business and Human Rights, European Journal of International Law, Volume 28, Issue 3, August 2017, Pages 899–919. Retrieved from: https://doi.org/10.1093/ejil/chx042

[1272] A/HRC/11/13, 22 April 2009, para. 71

[1273] UN Human Rights Council (2008). Promotion and protection of all human rights, civil, political, economic, social and cultural rights, including the right to development. Report of the Special Representative of the Secretary-General on the issue of human rights and transnational corporations and other business enterprises, John Ruggie. Available at: https://www.business-humanrights.org/sites/default/files/reports-and-materials/Ruggie-report-7-Apr-2008.pdf

[1274] More specifically it was defined as diligence 'reasonably expected from, and ordinarily exercised by, a person who seeks to satisfy a legal requirement or to discharge an obligation'.

[1275] Bonnitcha, J. and McCorquodale, R. The Concept of 'Due Diligence' in the UN Guiding Principles on Business and Human Rights. The European Journal of International Law Vol. 28 no. 3 EJIL (2017), Vol. 28 No. 3, 899–919 doi:10.1093/ejil/chx042 © The Author, 2017. Published by Oxford University Press on behalf of EJIL Ltd.

In respect to the financial sector, Worsdorfer finds that the actual human rights due diligence practices of the Equator Principles neither meet the minimum standards laid down in the UNGPs or the IFC Performance Standards.[1276] The current business and human rights regime at multinational banks has serious consequences for rights-holders. A perception that the Equator Principles are voluntary limits their impact due to a lack of proper enforcement, monitoring and sanctioning. As such, the literature demonstrates that the Principles are not able to prevent banks from financing projects containing serious human rights abuses.

In regards to cross-border effects, while the literature on effects of due diligence on host country state-governance capacity is sparse, opportunities are discussed. The 2005 OECD consultations on investment in weak-governance states only lightly touched on the ability of responsible multi-national company behaviour to contribute to state governance. However, the consultations concluded that both guiding principles by international organisations as well as policies designed by home governments of companies investing in foreign territory can and do play a role in helping weak governance countries develop healthier institutions (OECD, 2005). Furthermore, a 2018 study investigated the effects of two forms of U.S. due diligence (voluntary and mandatory) on foreign host country governance. In regards to voluntary due diligence, the study finds that the Electronic Industry Citizenship Coalition (EICC)'s Code of Conduct has caused changes in company behaviour beyond US companies, but likewise Taiwanese company behaviour. The study argues this change may demonstrate that due diligence might have been transplanted into Taiwan through private channels such as supply contracts, rather than through state governance. The study likewise finds that companies shift behaviour more prominently in response to the EICC code in comparison to the Dodd Frank Act suggesting that bottom- up approaches may be more effective or more easily accepted than state laws enacted by a foreign/national government in a top-down approach (Tsai & Wu, 2018). Finally, a 2014 study examines how states have responded to the emergence of forest and fisheries certification programs, arguing that while structural management differences are of influence, state responses typically demonstrate support by strengthening non-state program. While the study assesses effects on the forestry and fisheries sectors, results may be informative for state-governance shifts across sustainability issues (.Gulbrandsen, 2014).

[1276] Worsdorfer M. (2015). The Equator Principles and Human Rights Due Diligence – Towards a Positive and Leverage-Based Concept of Corporate Social Responsibility. Springer International Publishing. DOI: 10.1007/s40926-015-0014-6

Table 8.9: Literature on Challenges of HR Impacts of Voluntary Due Diligence Approaches

Study	Key Findings	Regulatory Option	Relevant Regulation	Source
Human Rights in the Void?	The effectiveness of the 'human rights due diligence' is in many respects dependent upon the moral commitment of corporations.	2	UNGP	Fasterling B., Demuijnck G., 2013.
The Concept of Due Diligence in the UN Guiding Principles on Business and Human Rights	While the UNGPs distinguish quite clearly what the expectations are for individual business operations versus those of actors along their value chain, they do not clarify when the different relationships apply (cause, contribute, directly linked). They additionally fail to indicate how far down the supply / value chain duties are to be implemented.	2	UNGP	Bonnitcha J. & McCorquodale R., 2017
The Equator Principles and Human Rights Due Diligence - Towards a Positive and Leverage-based Concept of Corporate Social Responsibility	The actual human rights due diligence practices of major (EP) FIs do neither meet the minimum standards laid down in the U.N. Guiding Principles on Business and Human Rights (and in the IFC Performance Standards).	2	Equator Principles; Leverage-based CSR; IFC Performance Standards	Worsdorfer M., 2015.
Governance of Mineral Supply Chains of Electronic Devices	Both Mandatory and Voluntary frameworks establish due diligence approaches. However, none of the approaches assessed are sufficiently transparent or credible in their implementation to infer any concrete implications for benefits to rights-holders.	2	UNGP	Sydow J., Reichwein A., 2018

Voluntary Certification Schemes and Conflict Minerals

Increasing focus on human rights due diligence— both voluntary and mandatory — created a unique and growing new market. While assurance and certification companies can be seen as tools for compliance with mandatory human rights due diligence requirements, such as the US Dodd-Frank Act, a plethora of certification schemes can also be defined as voluntary mechanisms focused on consumer information and perception of a product. This is particularly clear in the literature around conflict minerals, following the success of the Kimberley Process Certification Scheme in 2003. The extractive minerals industry is unique in the discussion of voluntary due diligence mechanisms for the benefit of rights-holders because of the difference in incentive structures for companies to prove their social sustainability to clients and consumers.

1) Initiative for Responsible Mining Assurance
2) Better Sourcing Program
3) International Tin Supply Chain Initiative (iTSCi)
4) CTC Standards Certification (BGR)
5) Conflict Free Gold Standard
6) Responsible Minerals Initiative
7) Fairtrade Gold Standard
8) Responsible Aluminium Stewardship
9) Responsible Business Alliance
10) Responsible Gold Guidance (LBMA)
11) Responsible Jewellery Council
12) SA 8000
13) Kimberley Process Certification Scheme
14) Global Reporting Initiative

However, focusing on actual human rights impacts, a study by German Watch, demonstrates that audits and certification schemes alone, even independent and high-quality ones, are not sufficient to ensure that an approach is credible and has any benefits for rights-holders.[1277] The following tables were put together to summarize the findings from German Watch's study demonstrating that while some voluntary due diligence practices in the mining industry ensure proactive compliance with an extensive set of human rights, the absolute effects are meaningless without credible and transparent reporting processes. The study developed a set of criteria to classify the levels of credibility and transparency among the voluntary certification schemes. The tables below demonstrate the human rights covered by each column of a certification scheme (in grey), and the level of credibility of each by the schemes represented by their highlighted colour at the top:

- Red: Not credible and transparent
- Yellow: Somewhat transparent, but not fully credible
- Green: Credible and transparent

[1277] Sydow J., Reichwein A. (2018). Governance of Mineral Supply Chains of Electronic Devices: Discussion of Mandatory and Voluntary Approaches in Regard to Coverage, Transparency and Credibility. Germanwatch e.V.

Table 8.10: HR Scope and Credibility of Voluntary Approaches

	Mines						3TG Minerals					More than 3TG or other Minerals					
	Voluntary Principles on Security and HR	International Council on Mining and Metals	Global Reporting Initiative	International Cyanide Management Code	SA 8000	IRMA	Better Sourcing Program	CTC Certification Standards	Conflict-free Gold Mining	Responsible Minerals Initiative	iTSCi	Fairtrade Gold Standard	Responsible Aluminium Stewardship	Responsible Business Alliance	Responsible Gold Guidance (LBMA)	Responsible Jewellery Council	DMCC
Forced Labour		■	■		■	■	■	■	■	■	■	■	■	■	■	■	
Human Trafficking	■		■		■	■	■		■			■	■	■		■	
Child Labour		■	■		■	■	■	■	■	■	■	■	■	■	■	■	■
Violence by State or Private Forces	■	■	■		■	■	■	■	■	■	■		■		■	■	■
Rape and Forced Prostitution			■		■	■	■		■	■	■	■	■		■		
Financing of Armed Groups					■	■	■	■	■	■	■	■	■	■	■	■	■
Workers' Rights – Health and Safety		■	■	■	■	■	■	■			■	■	■	■		■	
Workers' Rights – Fair Payment		■	■		■	■	■	■				■	■	■		■	
Workers' Rights – Health Insurance for Occupational Injuries		■	■		■	■						■		■			
Livelihood of local population		■	■		■	■	■	■				■	■			■	
Mining by locals			■		■	■						■	■			■	
Cultural Rights		■	■		■	■						■	■			■	
Forced Resettlement		■	■		■	■		■				■	■		■	■	
Compensation for Resettlement		■	■		■	■						■	■			■	

As is demonstrated by the tables above, the study communicates that numerous frameworks focus on specific issues, while others cover nearly all identified risks. However, the efficiency of these approaches is questionable as there are significant drawbacks regarding transparency of implementation and overall credibility. As such, companies conducting due diligence cannot be sure that human rights risks are legitimately addressed by the certified supplier. None of the assessed initiatives or guidelines met 100% of the criteria developed by German Watch to define it as fully credible and transparent. As such, the study concludes that the EU regulation on responsible mineral sourcing, or the US Dodd-Frank Act, must ensure that such schemes for accreditation provide for close monitoring to ensure that companies refrain from transferring their responsibility to protect rights-holders, and perform proper due diligence, to misleading certification schemes.

- **Mandatory Due Diligence**

Reporting Requirements

Reporting requirements, which require companies to report on their due diligence steps are common. Examples are found across industries and across jurisdiction at both sub-national and national levels. The existing literature reviews successful case studies and areas for possible expansion to enhance positive implications of reporting requirements including:

1) Section 1502 of the US Dodd-Frank Act;
2) California Transparency Act;
3) UK Modern Slavery Act
4) EU Non-Financial Reporting Directive. Directive 2014/95/EU. This directive lays down the rules on disclosure of non-financial and diversity information by large companies and makes it mandatory for companies to include non-financial statements in their annual reports from 2018 onwards.[1278]

The effectiveness of reporting requirements in increasing protection for rights-holders is a frequently debated topic. Much of the literature focuses on company-level impacts relating to compliance and transparency. However, reporting requirements are frequently perceived to be procedural requirements which do not lead to substantive impacts. According to the literature, when reporting and due diligence requirements are detailed and include requirements for collaboration with external stakeholders as well as compliance mechanisms they are more likely to create substantive impact.

[1278] European Commission Official Website. Accessed at https://ec.europa.eu/info/business-economy-euro/company-reporting-and-auditing/company-reporting/non-financial-reporting_en#companies-that-must-comply

Table 8.11: Literature on Positive HR Impacts of Mandatory Reporting Requirements as Due Diligence Approaches

Study	Key Findings	Regulatory Option	Relevant Regulation	Source
Hardening soft law: Are the emerging corporate social disclosure laws capable of generating substantive compliance with human rights?	Without any mechanism to encourage compliance with the legal requirements of transparency and due diligence, the uptake by companies of due diligence requirements may be limited. This has played out in practice via the implementation of the Modern Slavery Act in the UK. The introduction of civil (and criminal) penalties where human rights violations have occurred would significantly strengthen requirements.	3	US Dodd-Frank Act; California Transparency Act; UK Modern Slavery Act; French Duty of Corporate Vigilance Law	Nolan J., 2018
Source Intelligence; Conflict Minerals Appeals Court Ruling has No Impact on Filing Obligations	Companies' course of action is not necessarily affected by due diligence requirements such as the Dodd-Frank Act because they recognize public opinion is overwhelmingly in favour of transparency in the responsible production of goods.	3	US Dodd-Frank Act	Source Intelligence, 2014
Big Drop Reported in Child Labour in Cambodia Fashion Factories	Better Factories Cambodia, a U.N. International Labour Organization and World Bank initiative, found just 10 cases of child labour, down from 74 in 2014, in its latest survey of almost 500 licensed garment export factories. However, there are significant difficulties in formal reporting requirements of the informal sector.		N/A	Asia News Monitor, 2018
2018 Research Report. The state of corporate sustainability disclosure under the EU Non-Financial Reporting Directive[1279]	This study assessed whether companies provided the type of information explicitly required by the NFR Directive. The study finds that over 90% of companies express in their reports a commitment to respect human rights and over 70% endeavour to ensure the protection of human rights even in their supply chains. As in other areas, a majority of companies, however, do not provide any information that would allow a stakeholder to understand how this commitment is put		Directive 2014/95/EU	Alliance for Corporate Transparency, 2019

[1279] Alliance for Corporate Transparency. 2018 Research Report. The State of corporate sustainability disclosure under the EU Non-Financial Reporting Directive. The Alliance for Corporate Transparency project analysis of companies' reporting.(2019) Accessed at http://www.allianceforcorporatetransparency.org/

	into practice. Only 36% describe their human rights due diligence system, 26% provide a clear statement of salient issues and 10% describe examples or indicators to demonstrate effective management of those issues.			

While this report has reviewed a scarce pool of literature speaking to the positive implications of reporting requirements on human rights impacts, the literature on existing challenges is far more extensive. The existing literature reviews case studies and areas for possible improvement to mitigate negative implications of mandatory reporting requirements, including the UK Modern Slavery Act and the US Dodd-Frank Act.

According to an independent review led by Amnesty International, the UK Modern Slavery Act has failed to compel companies to respect their duties and implement proper due diligence. Weak monitoring and enforcement, of an already lenient reporting requirement, has allegedly meant that almost half of all companies under the legislation's jurisdiction have failed to publish a statement. While various companies have released a first statement, they are reported to have failed to follow up, and perceive the regulation as a procedural exercise rather than a substantive act. Unsurprisingly, the study finds that the most comprehensive reports are submitted by companies that were already engaged in conducting human rights impact assessments along their supply chain before the implementation of the Act.

Table 8.12: Literature on Challenges of HR Impacts of Mandatory Reporting Requirements as Due Diligence

Studies	Key Findings	Regulatory Option	Relevant Regulation	Source
Independent Review of the Modern Slavery Act - Joint Submission from Amnesty International UK, Anti-Slavery International, Business & Human Rights Resource CENTRE, core Coalition, Fairtrade Foundation, Freedom United and ShareAction	Three years on from its introduction, it is apparent that the legislation's impact is seriously limited by shortcomings in the reporting requirement, in combination with inadequate monitoring and enforcement.	3	UK Modern Slavery Act	Amnesty International UK; Anti-Slavery International; Business & Human Rights Resource Centre; CORE Coalition; Fairtrade Foundation; Freedom United and ShareAction. 2018.
Business and Human Rights in Brazil: exploring human rights due diligence and operational-level grievance mechanisms in the case of Kinross Paracatu gold mine	The biggest challenges in real impact for rights-holders lies on the inability of affected stakeholders to seek redress from a company that tries to excuse itself by showing compliance with policies based on internationally accepted procedures.	3		Turke M., 2018
Can we make them obey? US Reporting Companies, their Foreign Suppliers, and the Conflict Minerals Disclosure Requirements of Dodd-Frank	Until the international community collectively commits to end the conflict minerals trade, § 1502 and the SEC conflict minerals rule will not effectively achieve their intended benefits as due diligence burden will be passed down the levels of the supply chain rather than have significant benefits to rights-holders.	3		Harline M S., 2015
Workplace Human Rights Reporting: A Study of Australian Garment and Retail Companies	This research suggests that the soft disclosure regulation and oversight by the state, and the numerous failed attempts at introducing hard regulation, provide scope for corporations to avoid taking corrective action against human rights violations, if any. This study is unique as it shows that a soft regulatory environment, preserved by multiple failed attempts at introducing corporate human rights disclosure legislation, contributes to inadequate corporate disclosure practices.	3		Azizul Islam M., & Jain A., 2013
Big Drop Reported in Child Labour in Cambodia Fashion Factories	There are significant difficulties in formal reporting requirements of the informal sector.			Asia News Monitor, 2018

The literature likewise draws on a plethora of sector specific legislation to demonstrate gaps in compliance across countries. After its mission to Brazil in 2015, a United Nations working group report concluded that "human rights risks were mainly seen as risks to a company's operations, rather than risks faced by vulnerable rights-holders" (Turke M., 2018). According to a his study, the largest gold mine in Latin America, led by a Canadian company, shows policy commitment to human rights norms and due diligence requirements, but continues to be a cause of negative human rights impacts in the city of Paracatu, Brazil. While the company adheres to international guidance on human rights, local communities still claim to be impacted by health, infrastructural and environmental damages. According to Turke (2018), this demonstrates that without robust grievance mechanisms, reporting requirements are somewhat futile. Companies will aim to excuse themselves by pointing to procedural compliance and policies based on internationally accepted principles such as the UNGP (ibid.).[1280]

Similarly, a study by Deakin University and Queensland University of Technology investigated workplace human rights disclosure practices by 18 major Australian garment and retail companies that source products from developing nations.[1281] The investigators, Islam and Jain, found that the selected corporations only reported less than half of the specific disclosure categories. The research confirms arguments prominent in the literature that the lack of enforcement in mandatory reporting requirements provides space for corporations to only partially comply, and places impedes rights-holders' ability to benefit from such requirements.[1282]

Finally, and quite interestingly, Better Factories Cambodia, a joint initiative of the International Labour Organization and the International Finance Corporation (World Bank Group) initiative, found that child labour decreased significantly in Cambodia as an effect of reformed due diligence practices (Asia News Monitor, 2018). However, the study warns that there are significant difficulties in formal reporting requirements of the informal sector, as children turned away from monitored factory jobs may be pointed to work in homes and informally subcontracted to produce garments.

Judicial or economic penalties

The French National Assembly adopted the Duty of Vigilance Law in 2017, and accordingly it is too early to investigate its impacts on human rights. To date, France is the only country with a national law requiring general mandatory due diligence requirements of this scope. Similarly, the Netherlands adopted its Child Labour Due Diligence Law at the time of drafting of this report (May 2019). As a result, the literature on positive impacts of mandatory due diligence regulation as envisioned within the subject of this study is scarce.

However, longer established regulatory instruments which have certain similarities with these general due diligence duties may provide helpful comparisons, although the limitations resulting from their differences should be acknowledged. For example, Section 1502 of the US Dodd-Frank Act was signed into law in 2010, requiring publicly traded companies to ensure that the raw materials they use to make their products are

[1280] Turke M. (2018). Business and Human Rights in Brazil: Exploring Human Rights Due Diligence and Operational-Level Grievance Mechanisms in the case of Kinross Paracatu Gold Mine. Brazilian Journal of International Law. (Vol. 15, No. 2). DOI: 10.5102/rdi.v15i2.5357
[1281] Azizul Islam M., Jain A. (2013). Workplace Human Rights Reporting: A Study of Australian Garment and Retail Companies. Australian Accounting Review. (Vol 23, No. 65, Issue 2). doi: 10.1111/auar.12009
[1282] Ibid.

not tied to the conflict in Congo. The Enough Project conducted field research in 2015 and 2016 in Eastern Congo with miners, traders, human rights activists, civil society leaders, and foreign industry experts, to assess impacts of the legislation. The investigation found direct positive impacts including increased security for civilians in some mining areas and a significant reduction in armed group control in 3T mining areas. Additionally, a few indirect advances for rights-holders were found around improved safety and health standards for miners, and the implementation of a regional certification system for mines as conflict-free. When 193 mines were assessed under this certification scheme in Eastern Congo to investigate conflict and child labour, 166 of the mines (86%) successfully passed the assessment. Furthermore, according to the Enough Project (2015), the year 2015 saw a record amount of certified conflict-free tantalum exported from eastern Congo — a 387% increase since 2013. Moreover, looking at tin, tantalum, and tungsten mines together, 70% of those investigated by the International Peace Information Service in 2014 were conflict-free.

Despite these positive improvements on the ground, it is important to note that a study conducted by Global Witnesses and Amnesty International showed that many US companies are failing to comply with this mandatory due diligence. More specifically, the study analysed 100 conflict minerals reports filed by US companies in response to the 2010 Dodd Frank Act. This analysis found that 79 of these companies failed to meet the minimum requirements established by the law, that only 16% of them were going beyond their direct suppliers to attempt to contact those down the production chain, and that more than half of the companies sampled did not report to senior management when they identified a risk in their supply chain.[1283]

Concerning challenges, as mentioned above, existing examples of mandatory due diligence requirements for human rights and environmental impacts are rare. The primary example is the French Duty of Vigilance Law, which is too new to have generated information regarding its impacts.

As a result, this assessment is again reliant on the literature relating to examples of laws with comparative features. It is acknowledged that these comparisons have limited usefulness due to the narrower focus of these laws or the different kind of obligations which they create. Within this context, the literature demonstrates that the impacts for rights-holders could result in unintended consequences when mandatory due diligence obligations are imposed only for certain geographical regions, allowing businesses to move to other areas of supply where these due diligence requirements do not apply. While the UNGPs make explicitly clear that due diligence should not lead companies to terminate their business in a specific region, but rather exercise leverage to try and improve conditions, the literature demonstrates where the law does not apply to a company's global operations, it does indeed risk the movement of businesses.This has been the case for the US Dodd Frank act. As a study by the University of Texas School Of Law suggests, Section 1502 of the Dodd-Frank Act has essentially created a de facto embargo on the entire mining industry in the DRC. Companies found it simpler to withdraw from the area rather than to justify business associations with conflict. This sudden change caused the demand of minerals in the area to drop by 90%, placing the economic burden on a vast population of civilians that depended on the market's income

[1283] Amnesty International and Global Witness. Digging for Transparency. How US companies are only scratching the surface of conflict minerals reporting (2015) Accessed at https://www.globalwitness.org/en/campaigns/conflict-minerals/digging-transparency/

for their livelihood. According to the study, this has had negative impacts relating to the right to food, the right to education, and the right to health.[1284] Furthermore, research from the UN Group of Experts report on the Congo found that gold from mines controlled by rebel groups such as Nduma Defense of Congo (NDC) headed by Ntabo Ntaberi Sheka who is wanted by Congolese authorities for crimes against humanity, was smuggled into Uganda last year.[1285] However, this phenomenon could presumably be linked to the mechanism's narrow application to a specific geographical region, which may not apply if the due diligence requirements were imposed on a wider group of businesses operating globally.

[1284] Owen M. (2013). The Limits of Economic Sanctions Under International Humanitarian Law: The Case of the Congo. Texas International Law Journal. (Vol. 48., No. 103)

[1285] Amnesty International and Global Witness. Digging for Transparency. How US companies are only scratching the surface of conflict minerals reporting (2015). Page 32. Accessed at https://www.globalwitness.org/en/campaigns/conflict-minerals/digging-transparency/

Table 8.13: Literature on Challenges of HR Impacts of Mandatory Due Diligence Approaches

Study	Key Findings	Regulatory Option	Relevant Regulation	Source
The Kimberley Process Certification System - KPCS and Diamond Production Changes in Selected African Countries and Brazil	In summary, the KPCS imposed control and, in response, abuses implemented by the industry financed government have not been mitigated while various crimes have emerged in the move of diamonds to the informal market such as; smuggling; illegal production; invasion of indigenous lands and environmental reserves; disrespect to environmental legislation; robberies; deaths and other crimes.	4.1 / 4.3 (b)	KPCS	Gomes dos Santos E., 2015
Unintended Consequences of Sanctions for Human Rights: Conflict Minerals and Infant Mortality	While meant as a boycott on products that may finance warlords and armed militias, the study suggests that the legislation-induced boycott reduced mothers' consumption of infant health care goods and services.	4.1 / 4.3 (b)	Dodd-Frank Act	Parker D., Foltz J., Elsea D., 2016
The Limits of Economic Sanctions Under International Humanitarian Law: The Case of the Congo	The withdrawal of international corporations from the Congo has reduced the legitimate minerals trade by ninety percent, penalizing hundreds of thousands of civilians across the Great Lakes region who depend on this trade for their livelihood.	4.1 / 4.3 (b)	Dodd-Frank Act	Owen M., 2013
The elephant in the room: offshore companies, liberalisation and extension of presidential power in DR Congo	The study notes that while the Congolese government voiced support for the Dodd-Frank Act, donors continued to hold reservations regarding government behaviour. However, despite such reservations, they continued to operate in Congo on the basis that it was a special case for the need to safeguard international investment in a wider sense.		Dodd-Frank Act	Marriage, 2017
What Conflict Minerals Rules Tell us About the Legal Transplantation of CSR Standards without the State: From the UN	This study investigates the effects of two forms of U.S. due diligence (voluntary and mandatory) on foreign host country governance. In regards to mandatory due diligence, the study finds that the Dodd-Frank Act is less effective in shifting governance capacity of the		Dodd-Frank Act	Tsai & Wu, 2018

to the US to Taiwan	host country as domestic companies change behaviour less prominently than in comparison to voluntary guidelines. The study suggests that bottom- up approaches may be more effective or more easily accepted than public standards such as state laws enacted by a foreign/national government in a top-down approach.			

A 2016 study by the University of Wisconsin-Madison confirmed this argument, outlining that while the conflict-minerals section of the 2010 Dodd-Frank Act has succeeded in its mission of decreasing the financing of warlords and conflict in East Congo, it has also had unexpected negative effects on rights-holders in the area.[1286] By dis-incentivizing companies from sourcing tin, tungsten, and tantalum from the Congo, the Act placed somewhat of a de facto boycott on mineral purchases. Estimating the impact on the mortality of children born before 2013, the study finds that it increased the probability of infant deaths in villages near the policy-targeted mines by at least 143 percent. Similarly to the literature on burden allocation of economic sanctions, the paper suggests that the Act's boycott reduced mothers' means to purchase health care goods and services for their infants.[1287] What is more, another recent study has suggested that for territories with an average number of gold mines, the introduction of Dodd-Frank increased the incidence of battles with 44%; looting with 51% and violence against civilians with 28%, compared to pre-Dodd Frank averages.[1288] However, the evidence on positive versus negative impacts of the Dodd-Frank Act is inconclusive as some studies are argued to exaggerate positive impacts, while others are claimed to exaggerate negative impacts. An August 2018 study by Radboud University found that academic studies investigating negative unintended consequences of the Dodd-Frank Act in the Congo are largely relying on outdated and skewed data. The authors argue that while negative unintended effects were declining in the region, companies that stood to gain from deregulation omitted such changes from their records (Koch & Kinsbergen, 2018).

Beyond legislation such as the US Dodd-Frank Act, there have also been prior attempts to include processes to protect the environment and human rights when companies operate on the ground using certification schemes. One of the most notable ones has been the Kimberley Process. The Kimberley Process is a multilateral trade regime established in 2003 with the goal of preventing the flow of conflict diamonds. The core of this regime is the Kimberley Process Certification Scheme, under which States implement safeguards on shipments of rough diamonds and certify them as conflict free.[1289] Under this certification scheme the member states must ensure that the diamonds that must be exported with a Kimberley Process Certificate should not finance rebel groups, and that none of the diamonds imported to their country come from a non-member of the scheme. This translates into the need for countries to establish legislation, institutions, and import/export controls,[1290] but unlike the due diligence requirements we have outlined before, the certification scheme does not impose requirements specifically on businesses. This puts governments in a difficult position as they must penalize the companies that are at the same time funding their existence via the payment of ludicrous taxes, particularly in countries where a high percentage of government revenues come from the extractive sector, for instance in Nigeria, the extractives sector has represented 74% of the government revenue at some points.[1291]

[1286] Parker D., Foltz J., Elsea D. (2016). Unintended Consequences of Sanctions for Human Rights: Conflict Minerals and Infant Mortality. Journal of Law and Economics (Vol. 59). University of Chicago.
[1287] Parker D., Foltz J., Elsea D. (2016). Unintended Consequences of Sanctions for Human Rights: Conflict Minerals and Infant Mortality. Journal of Law and Economics (Vol. 59). University of Chicago.
[1288] Stoop N, Verpoorten M, van der Windt P (2018) More legislation, more violence? The impact of Dodd-Frank in the DRC. PLoS ONE 13(8): e0201783. https://doi.org/10.1371/journal.pone.0201783
[1289] Kimberley Process Official Website.Last accessed May 31st 2019. Accessed at https://www.kimberleyprocess.com/en/what-kp
[1290] Ibid.
[1291] UNCTAD. Extractive Industries: Optimizing value Retention in Host Countries. (2012) Accessed at https://unctad.org/en/PublicationsLibrary/suc2012d1_en.pdf

However, and despite the creation of these schemes, literature reflects that the reach of sector-specific due diligence requirements via certification schemes fail to mitigate human rights abuses when they stem from publicly-owned companies. According to Gomes dos Santos, the scope of the Kimberley Process Certification Scheme (KPCS) does not extend to protect from violations committed by the member states themselves who are financed by the industry.[1292] Drawing on Zimbabwe as a case study, the author demonstrates that while the KPCS has been implemented with the intention of protecting rights-holders, the control imposed by the scheme (need to apply for permits and pay the required fee) continued to finance the national government accused of human rights abuses, while likewise driving the diamond trade further onto the illegal market. The lack of oversight caused by increased transactions under the illegal market incentivized the use of illegal production methods, trespassing on protected land, ignorance of environmental protection standards, and violent crimes including robbery. Similar to the effects of the Dodd-Frank Act on the livelihoods of legitimately practicing traders, the KPCS also caused those formally employed in the diamond production chain to decrease from almost 4,000 to about 650 in 2009.[1293]

Mandatory Due Diligence Relating to Conflict Minerals

In regard to sector-specific mandatory due diligence of conflict minerals, the German Watch study referred to above considers the US Dodd-Frank Act (1502) and the EU regulation on responsible mineral sourcing as the most far-reaching.[1294] However, they are both relatively new frameworks and have significant shortcomings. In terms of the US Dodd-Frank Act, only companies listed on the New York Stock Exchange are required to ensure that minerals sourced only from the Great Lakes region do not finance conflicts. Those that bring in Internet Technology (IT)-products via the European market are not subject to any checks and are not required to conduct due diligence.

In contrast, the EU regulation on responsible mineral sourcing applies to European smelters and importers of primary materials. Importers must allow external due diligence to be conducted by union importers. However, these efforts to enact industry-specific certification and due diligence schemes can only protect rights-holders down the supply chain if the requirements are enforced across borders.

In regards to cross-border effects, the literature on effects of due diligence on host country state-governance capacity is sparse. A 2017 study on the link between multinational companies and the Congolese presidency notes that while the Congolese government voiced support for the Dodd-Frank Act, donors continued to hold reservations regarding government behaviour. However, despite such reservations, they continued to operate in Congo on the basis that it was a special case for the need to safeguard international investment in a wider sense (Marriage, 2017). A further study assessed the effects of two forms of U.S. due diligence (voluntary and mandatory) on foreign host country governance. In regards to mandatory due diligence, the study finds that the Dodd-Frank Act is less effective than voluntary guidelines in shifting governance capacity of the host country as domestic companies more prominently change behavior

[1292] Gomes dos Santos E. (2015). The Kimberley Process Certification System – KPCS and Diamond Production Changes in Selected African Countries and Brazil. Geosciences, 68(3), pp. 279-285.
[1293] Kimberley Process Official Website.Last accessed May 31st 2019. Accessed at https://www.kimberleyprocess.com/en/what-kp
[1294] Sydow J., Reichwein A. (2018). Governance of Mineral Supply Chains of Electronic Devices: Discussion of Mandatory and Voluntary Approaches in Regard to Coverage, Transparency and Credibility. Germanwatch e.V.

when exposed to voluntary guidelines in comparison. The study suggests that bottom-up approaches may be more effective or more easily accepted than state laws enacted by a foreign/national government in a top-down approach (Tsai & Wu, 2018).

Table 8.14: HR Scope of Mandatory Due Diligence Regulation

	Conflict Minerals					
	EU Regulation on Responsible Mineral Sourcing	Dodd Frank 1502	International Conference on the Great Lakes Regional Certification	Health in Mines ILO Convention	Minamata Convention on Mercury	ILO Indigenous and Tribal People Convention 169
Forced Labour						
Human Trafficking						
Child Labour						
Violence by State or Private Forces						
Rape and Forced Prostitution						
Financing of Armed Groups						
Workers' Rights – Health and Safety						
Workers' Rights – Fair Payment						
Workers' Rights – Health Insurance for Occupational Injuries						
Livelihood of local population						
Mining by locals						
Cultural Rights						
Forced Resettlement						
Compensation for Resettlement						

The report likewise noted various pieces of legislation that have the demonstrated capacity to bridge the obvious gaps, if appropriately enforced: the EU Non-Financial Reporting Directive, the French Duty of Vigilance Law, the UK Modern Slavery Act, and the California Transparency in Supply Chains Act. However, it is noted that apart from the French law these examples contain reporting requirements without enforcement of substantive due diligence standards.

1.4 Environmental Impacts

Businesses carry out their environmental due diligence processes to ensure that their company complies with environmental protection regulations both to protect the environment and to protect the health and safety of workers and communities.

Companies carry out this due diligence to ensure that the company's operations as well as its subcontractors' are in line with the law and with internal corporate guidelines vis-à-vis the environment. Even beyond existing environmental and health risk regulations, environmental due diligence is used to understand potential risks and potential obligations that may derive from the businesses' actions to prevent potential future liability derived from their operations.

However, drawing again on the distinction highlighted by Bonnitcha and McCorquodale above, the corporate use of the phrase "due diligence" for compliance with laws does not mean that these laws require due diligence as a standard of care in the way envisioned by the French Duty of Vigilance Law.[1295] Indeed, as set out elsewhere in this study, the French law currently forms the primary existing example of a law which imposes due diligence as a legal standard of care for companies' environmental impacts. However, in the absence of meaningful information about the implementation impacts of this new law, this study again focuses on laws which have certain comparative features, whilst acknowledging their differences.

Due diligence has traditionally involved risk prevention and management, especially to ensure that new acquisitions would not bring along potential risks to the company. However, due diligence has evolved to encompass the company's environmental footprint and its operational effect on surrounding populations.1296 Along these lines, regulations such as Directive 2011/92/EU and Directive 2001/42/EC, have started requiring for companies to carry out environmental impact assessments (EIAs), sustainability impact assessments (SIAs) and, more recently, human rights impact assessments (HRIAs).

This evolution and the insertion of human rights due diligence, beyond the requirements for business of HRIAs as a onetime activity, have environmental implications. Firstly, because the right to a healthy environment is recognized as a human right, and secondly because the enjoyment of many other human rights requires a healthy environment. Examples of human rights which are interrelated with the environment include the right to health, the right to life, the right to food, the right to safe working conditions, the right to water, and so forth.[1297] Many human rights instruments and national constitutions include the right to a healthy environment, and acknowledge that a safe, healthy and sustainable environment is integral to the full enjoyment of a wide range of human rights, and that without a healthy environment, we would not be able to achieve minimum standards of human dignity.[1298] Building on this recognition of the interrelated relationship between human rights and the environment, the UN Human Rights Council established a mandate on human rights and the environment in 2012. This mandate has been further extended in 2018[1299], for the Special Rapporteur to continue "helping to clarify the relationship between human rights and the environment".[1300] Countries such

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[1295] Jonathan Bonnitcha, Robert McCorquodale, The Concept of 'Due Diligence' in the UN Guiding Principles on Business and Human Rights, European Journal of International Law, Volume 28, Issue 3, August 2017, Pages 899–919. Retrieved from: https://doi.org/10.1093/ejil/chx042
[1296] Geordan Graetz & Daniel M. Franks (2013). Incorporating human rights into the corporate domain: due diligence, impact assessment and integrated risk management, Impact Assessment and Project Appraisal, 31:2,97-106, DOI: 10.1080/14615517.2013.771006
[1297] Article 25 of the 1948 Universal Declaration of Human Rights
[1298] OHCHR, 2019. Accessed at https://www.ohchr.org/EN/Issues/Environment/SREnvironment/Pages/SRenvironmentIndex.aspx
[1299] A/HRC/RES/37/8. Accessed at https://documents-dds-ny.un.org/doc/UNDOC/GEN/G18/099/17/PDF/G1809917.pdf?OpenElement
[1300] A/HRC/RES/37/8 page 3. Accessed at https://documents-dds-ny.un.org/doc/UNDOC/GEN/G18/099/17/PDF/G1809917.pdf?OpenElement

as France and the Netherlands have introduced more general due diligence regulations that include an environmental dimension.

As can be seen from the Market Practice section, current due diligence practices include aspects of the environment such as air pollution, greenhouse gas emissions, biodiversity and climate change. Nevertheless, in the area of international investment arbitration, the process to introduce regulations and enact new policies that take into account the relationship between human rights and environmental protection is met with resistance from businesses and even some governments. An increasing amount of disputes are being brought to international arbitration by investors and businesses that see changes in policy to increase environmental (and by implication human rights) protection as a violation of the conditions under which they agreed to develop their businesses and as a breach of the investment treaties protecting them. Companies argue, amongst other things, that these regulations hamper their pre-established operations or increase their operating costs in an unprecedented manner. On the other hand, governments are concerned about the environmental costs and the proper protection of their citizens' basic human rights. As an example of the magnitude of these costs, it has been estimated that governments have paid corporations nearly US $400 million in the settlement of disputes under North American Free Trade Agreement (NAFTA) concerning environmental and health related laws.[1301] It has also been estimated that Canada has paid US $200 million[1302] to US investors in the settlement of arbitration disputes mostly related to environmental protection or resource management that had negatively affected the corporations' profits.

Moreover, businesses are attempting to sue governments, or threatening to do so, even before they have an operating mine on site[1303] for damages to their investment that derive proposals to prioritize the protection of human rights and the environment, which would impose new duties to investors in these areas. For instance, in the case of Carmichael Coal (also known as Adani) a coal mine faced strong backlash from society and environmental activists in Australia even before the operations started. The company recently released a statement by which it threatened with a multi-billion dollar lawsuit if the government agreed to the citizens' petitions to stop the mine.[1304] Furthermore, a recently released report by Mining Watch Canada that studied 38 cases filed by mining corporations against Latin American Governments via the investor-state dispute settlement (ISDS) system noticed that a "majority of these cases were brought by exploration companies that have no operating mine, or no other mining project at all, (…) in several cases, (Infinito Gold v. Costa Rica, Eco Oro Minerals v. Colombia, and TriMetals Mining - formerly South American Silver- v. Bolivia), exploration companies were being backed by third party funders who would profit from the case if the arbitration panel finds in favor of the company".[1305] This allows companies to try to sue the governments without risking losses if they do not win the case, while governments

[1301] Bernstein, Jared. "Trump's preliminary deal with Mexico is better for workers on both sides of the border than prior trade deals". The Washington Post. August 28 2018. Accessed at: https://www.washingtonpost.com/news/posteverything/wp/2018/08/28/trumps-preliminary-deal-with-mexico-is-better-for-workers-on-both-sides-of-the-border-than-prior-trade-deals/?utm_term=.4179c0b45010
[1302] This amount does not include legal fees that have been estimated to total nearly $65 million for these cases.
[1303] Moore, J. and Perez Rocha, M. Mining Companies Gambling with Latin American Lives and Sovereignty through Supranational Arbitration. Mining Watch Canada, Institute for Policy Studies and CIEL. 2019. Accessed at: https://miningwatch.ca/sites/default/files/isds_report_final_.pdf
[1304] Owens, Jared. Adani to seek billions if mine blocked. March 4th 2019. The Australian. Accessed at https://www.theaustralian.com.au/nation/politics/adani-to-seek-billions-if-mine-blocked/news-story/2a60e77c8214efe4e4fede033e47ea14
[1305] Moore, J. and Perez Rocha, M. Extraction Casino. Mining companies Gambling with Latin American Lives and Sovereignty through supranational aribrtration. Mining Watch, Institute for Policy Studies and CIEL. (2019). Page 3.

have to spend millions of dollars in their defense that will not be recovered even if the government wins the case.

Originally these controversies and concerns were also expressed in the EU policy-making process on environmental due diligence. The process leading to the enactment of the EU Timber Regulation was met with scepticism by a coalition of forest-rich countries (Austria, Germany, Finland and Sweden) that initially opposed the insertion of such environmental safeguards.[1306] This coalition encountered a coalition of countries, mostly timber import-dependent (the UK, the Netherlands and Denmark) that supported the regulation. After two years of political negotiations, there were expressions of a widespread perception that the policy would not mean a revolution but rather a political signal[1307] to point out that illegal logging is forbidden.[1308] The regulation continued to introduce due diligence mechanisms which were subsequently complemented by the EU Non-Financial Reporting Directive (2014/95/EU) and the EU Conflict Minerals Regulation (Regulation 2017/821). The former requires large companies to report on their impacts and risks regarding human rights and environment, amongst other matters. The latter applies to the tin, tantalum, tungsten and gold industries, and establishes the obligation for EU importers to carryout due diligence as from 2021.

Furthermore, the 2016 Council Conclusions on Business and Human Rights called for the launch of an EU Action Plan on Responsible Business Conduct. Political groups[1309] are calling for the implementation of the UNGPs across the EU policy framework. In addition, some Member States, such as France, are taking the lead by enacting laws that impose general human rights and environmental due diligence requirements. According to the 2017 French Duty of Vigilance Law, the company must draft a vigilance plan that "includes due diligence measures to identify risks and prevent serious violations of human rights and fundamental freedoms, human health and safety, and the environment (…)".[1310] (See Country Report on France in Regulatory Review above.) Civil society organisations and claimants which are of the view that a company' vigilance plan does not adequately address adverse impacts to human rights and the environment may formally ask for the companies to explain the shortcomings or approach a court.

As is evidenced in the Regulatory Review of this study, calls or proposals for similar laws which impose mandatory due diligence as a legal standard of care for human rights and environmental harms are currently in varied stages of being considered in Germany, Finland, the UK and other EU Member States, as well as in Switzerland.

1.4.1 Pre-Implementation Impact Assessment Review

[1306] Sotirov et al. The emergence of the European Union Timber Regulation: How Baptists, Bootleggers, devil shifting and moral legitimacy drive change in the environmental governance of global tinder trade. Forest Policy and Economics. Volume 81, August 2017, Page 69-81. Accessed at https://doi.org/10.1016/j.forpol.2017.05.001

[1307] Quote from Sotirov. Et al. (2017), page 76. "When a perception developed that the EUTR would not mean a revolution and the prohibition would be more of a symbolic policy for the forest sector, sending out a political signal to the public that policymakers care about the issue (C1, C2), political support of the EUTR was reached in the Council. The normative power of environ-mental and economic arguments convinced most Member States to vote in favour once it became unlikely that the EUTR could be stopped: "To simply forbid it [illegal logging] - yes, this is charming, I have to admit this. And you can nicely sell this"

[1308] Sotirov et al. The emergence of the European Union Timber Regulation: How Baptists, Bootleggers, devil shifting and moral legitimacy drive change in the environmental governance of global tinder trade. Forest Policy and Economics. Volume 81, August 2017, Page 75-76. Accessed at https://doi.org/10.1016/j.forpol.2017.05.001

[1309] The MEPS for responsible business conduct has created a Shadow plan Accessed at https://responsiblebusinessconduct.eu/wp/

[1310] PROPOSITION DE LOI relative au devoir de vigilance des sociétés mères et des entreprises donneuses d'ordre. http://www.assemblee-nationale.fr/14/ta/ta0924.asp

The table below reviews environmental impacts found in impact assessments carried out prior to the implementation of relevant EU regulations. A common feature across these evaluations is that the quantification of the effects on the environment is addressed in general terms, particularly in the case of illegal extraction and trade activities, which are difficult to trace. Environmental impacts often include indirect positive effects derived from changes in companies' conducts due to reputational concerns, and from changes in market flows – i.e. re-channeling demand and supply flows from and to compliant agents.

The review commences with the European Commission's Impact Assessment on Additional Options to Combat Illegal Logging (2008) mentioned above. As detailed above, EU policy regarding illegal logging was set out in the Forest Law Enforcement, Governance and Trade (FLEGT) Action Plan which assessed five additional measures to the original VPA approach including 1) expansion of the FLEGT VPA approach; 2) Further development of voluntary measures by the private sector; 3) Border measures to prevent the importation of illegally harvested timber; 4A) Legislation which prohibits the trading and possession of timber and timber products harvested in breach of the laws of the country of origin; 4B) Legislation which requires that only legally harvested timber and timber products be placed on the market. Under all policy options, the volume of illegal logging was expected to reduce and as such also decrease destructive practices such as high-grading, soil and stand damage; depletion of the forest resource base and threatening remaining intact sites; deforestation, erosion sedimentation and variations in hydrological regimes that lead to degradation of land and water resources; loss of forest cover due to informal roads constructed by illegal loggers; and recurrent forest fires. Under Option 1, however, the licensing scheme would expand which is expected to simultaneously increase harvesting volumes—putting more pressure on the environment, albeit this change would be moderate. This is likewise applicable to Option 2 where destructive practices are expected to decrease on the assumption that the private sector schemes reduce illegal logging and increase legal supply. Under Policy Option 3, which proposes border measures to prevent the importation of illegally harvested timber, illegal logging volumes are also expected to decrease among those countries with high or moderate risk. The trade analysis suggests that there would be a slight decline in the overall timber price leading to an increase in the profitability of other land uses – i.e. increases in forest conversion. Expected impacts under policy options 4 – 5 can all expect decreases in detrimental environmental practices, where in policy option 4, mitigation impacts will be most felt domestically among countries where illegal logging already occurs, and options 4B and 5 would expect explicit improvements in adherence to environmental regulations.

The table follows by reviewing the environmental impacts of the EU Commission Impact Assessment of EU NFRD Proposal (2013). The EU NFRD was proposed in the frame that disclosure requirements had not yet covered aspects of significance regarding environmental sustainability. A key motivation for the EU NFRD proposal was the longstanding transparency issues in corporate responsibility towards the environment. The Impact Assessment reviewed five possible policy options including 1) voluntary annual statements; 2) mandatory detailed, stand-alone non-financial reporting; 3) non-financial report on a "report or explain" basis; 4) voluntary reporting; 5) mandatory EU standard. Under both policy options 1 and 2a, which are the assessments preferred options, environmental awareness is expected to increase via improved transparency and better quality of information on companies' environmental performance. This would have an indirect positive environmental impact by increasing peer pressure and raising reputational costs for misbehaviour, which would lead to improvements on businesses' conduct.

Thereafter, we investigate the EU Assessment of Due Diligence Compliance Cost, Benefit and Related Effects on Selected Operators in Relation to the Responsible Sourcing of Selected Minerals (2014), for the relevant environmental impacts of six policy options regulating such activity including 1) Standalone EU Communication; 2) a "soft-law" approach; 3) Voluntary regulation establishing obligations under an "EU responsible importer" certification based on the OECD Guidance; 4) Mandatory regulation establishing obligations under an "EU responsible importer" certification based on the OECD Guidance; 5) a directive establishing obligations for EU-listed companies based on the OECD Guidance; and 6) an import ban when EU importers of ores fail to demonstrate compliance with the OECD Guidance. Under the current scenario, there is inexistent support for the development of sustainable economic models relying on natural resource wealth and transparent extractive sectors. While there are no specific impacts on the environment under options 1 or 2, option 3 is expected to have indirect positive environmental impacts based on reputation as this option would encourage demand for ethically and legitimately sourced minerals, leading to formalised mining sectors, more sustainable development and environmental protection. However, similarly to the impacts on human rights outlined above, policy options 4 and 5 risk being ineffective as companies may seek the easiest, least risky and burdensome way of complying (avoiding sourcing from conflict-affected regions). This could trigger negative impacts on the environment as mineral flows could be diverted towards companies with lower environmental standards and norms. Finally, policy option 6 is expected to deliver indirect positive effects through increased government interventions to ensure that due diligence on environmental impacts is exercised.

The EU Impact Assessment of Directive 2008/99/EC on the protection of the environment through criminal law, which lays down a list of environmental offences that must be considered criminal offences by all Member States if committed intentionally or with serious negligence, then reviews three policy options, with the first being no action at the EC level. The second policy option consists of encouragement for cooperation between Member States, and the third explored option regards minimum regulatory standards. While the first option is not foreseen to have negative or positive impacts, option 2 and 3 are expected to benefit efforts for environmental protection due to increased awareness amongst public authorities, investigators, prosecutors and judges, as well as citizens. While specifically under option 2, judges may make better use of the sanctions available under national legislations, policy option 3 goes a step further and increases the ability to harmonize sanction levels, offence definitions, and scope of liability across member states.

Lastly, we sought to investigate the results of the pre-implementation EU Impact Assessment of the Seveso III Directive for any environmentally relevant impacts. While the directive investigates six policy options, there was no detailed assessment of environmental impacts available.

Table 8.15. Impact Assessments carried out prior to the implementation of regulation with potential environmental impacts

Pre-implementation Impact Assessments	Environmental Impacts
EU Commission Impact Assessment on Additional Options to Combat Illegal Logging (2008)[1311,1312]	
Baseline scenario	The VPA licensing scheme would reduce the volume of illegal logging, avoiding destructive practices such as: • high-grading, soil and stand damage; • depletion of the forest resource base and threatening remaining intact sites; • deforestation, erosion sedimentation and variations in hydrological regimes that lead to degradation of land and water resources; • loss of forest cover due to informal roads constructed by illegal loggers; • and recurrent forest fires.
Option 1 – Expansion of the FLEGT VPA approach	As in the baseline scenario, destructive practices linked to illegal logging would be reduced. With the expansion of the licensing scheme, the harvesting volumes would increase and put more pressure on the environment, however, this change would be moderate.
Option 2 – Voluntary measures by the private sector further developed	The assessment for the baseline scenario applies if the private sector schemes reduce illegal logging and increase legal supply.
Option 3 – Border measures to prevent the importation of illegally harvested timber	The assessment for the baseline scenario applies to all countries with high or moderate risk of illegal logging. The trade analysis suggests that there would be a slight decline in the overall timber price leading to an increase in the profitability of other land uses – i.e. increases in forest conversion.
Option 4A – Legislation which prohibits the trading and possession of timber and timber products harvested in breach of the laws of the country of origin	The assessment for the baseline scenario concerning overall environmental impact applies. The positive impacts of eliminating illegal logging extend to those EU Member States where illegal logging occurs.
Option 4B – Legislation which requires that only legally	The assessment for the baseline scenario concerning overall environmental impact applies; there

[1311] See COMMISSION STAFF WORKING DOCUMENT Accompanying document to the Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL determining the obligations of operators who make timber and timber products available on the Market. IMPACT ASSESSMENT Report on additional options to combat illegal logging. Available at: https://ec.europa.eu/environment/forests/pdf/impact_assessment.pdf

[1312] Indufor (2008). Assessment of the impact of potential further measures to prevent the importation or placing on the market of illegally harvested timber or products derived from such timber. Final Report. [online] Helsinki, Finland: Indufor in association with European Forest Institute (EFI). Available at: https://ec.europa.eu/environment/forests/pdf/ia_report.pdf [Accessed 10 Sep. 2019].

harvested timber and timber products to be placed on the market	would also be an improvement in adherence to environmental regulations.
Option 5 – Legislation requiring companies placing timber and timber products on the market to exercise due diligence in ascertaining that the products are legal	Similar impacts to Option 4B.
EU Commission Impact Assessment on EU NFRD Proposal (2013)[1313]	
Option 0 – No policy change	No negative effects but also not beneficial impact.
Option 1 – Requiring a statement in the Annual Report	• More transparency; • better quality of information on companies' environmental performance; • increase in environmental awareness; • increase in reputational costs for misbehaviour
Option 2a – Requiring a detailed, stand-alone non-financial report on a mandatory basis	Similar impacts to Option 1.
Option 2b – Requiring a detailed non-financial report on a "report or explain" basis (companies are allowed to explain why they have not reported).	The report only provides a preliminary assessment of environmental impacts for the preferred options: Option 1 and Option 2a.
Option 2c – Voluntary reporting	
Option 3 – Setting up a mandatory EU standard	
EU Conflict Minerals – Assessment of Due Diligence Compliance Cost, Benefit and Related Effects on Selected Operators in Relation to the Responsible Sourcing of Selected Minerals (2014)[1314]	

[1313] See COMMISSION STAFF WORKING DOCUMENT IMPACT ASSESSMENT Accompanying the document Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL amending Council Directives 78/660/EEC and 83/349/EEC as regards disclosure of non-financial and diversity information by certain large companies and groups. Available at https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52013SC0127

[1314] See European Commission (2014), Impact Assessment Accompanying the document Proposal for a Regulation of the European Parliament and of the Council setting up a Union system for supply chain due diligence self-certification of responsible importers of tin, tantalum and tungsten, their ores, and gold originating in conflict-affected and high-risk areas. PART 1 (Impact Assessment). Available at: https://eur-lex.europa.eu/resource.html?uri=cellar:b05a9c8f-a54d-11e3-8438-01aa75ed71a1.0001.01/DOC_1&format=PDF

Baseline scenario	Inexistent support for the development of sustainable economic models relying on natural resource wealth and transparent extractive sectors.
Option 1 – Standalone EU Communication	This option does not create any specific impact on the environment.
Option 2 – "Soft-law" approach	Similar impacts to Option 1.
Option 3 – Regulation establishing obligations under an "EU responsible importer" certification based on the OECD Guidance (Voluntary)	Indirect benefits based on reputation. This option would encourage demand for ethically and legitimately sourced minerals, leading to formalised mining sectors, more sustainable development and environment, and benefits for local communities.
Option 4 – Regulation establishing obligations under an "EU responsible importer" certification based on the OECD Guidance (Mandatory)	Companies may seek the easiest, least risky and burdensome way of complying (avoiding sourcing from conflict-affected regions). This could trigger negative impacts on the environment as mineral flows could be diverted towards companies with lower environmental standards and norms.
Option 5 – Directive establishing obligations for EU-listed companies based on the OECD Guidance	Similar impacts to Option 5.
Option 6 – Prohibition of imports when EU importers of ores fail to demonstrate compliance with the OECD Guidance (Import ban)	Indirect positive effects through increased government interventions to ensure that due diligence is exercised.
EU Impact Assessment of Directive 2008/99/EC on the protection of the environment through criminal law[1315]	
Option 1 – No action on EC level	No negative effects but also not beneficial impact.
Option 2 – Encourage cooperation between Member States	Positive impact on the protection of the environment due to an increased awareness amongst public authorities, investigators, prosecutors and judges, as well as citizens. For example, judges may make better use of the sanctions available under their national legislations.
Option 3 – Set minimum regulatory standards	Positive impact on the protection of the environment due to the following: • High level of public awareness and political agreement.

[1315] See COMMISSION STAFF WORKING DOCUMENT Accompanying document to the Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on the protection of the environment through criminal law. IMPACT ASSESSMENT. Available at: https://ec.europa.eu/smart-regulation/impact/ia_carried_out/docs/ia_2007/sec_2007_0160_en.pdf [Accessed 11 Sep. 2019].

	• Increased sanction levels, broader definitions of offences, and extended scopes of liability (e.g. the liability of the legal person does not rule out personal liability).
EU Impact Assessment of Directive 2012/18/EU – Seveso III Directive[1316]	
Policy Issue 1 – Alignment of Annex I to CLP	Environmental impacts were not assessed in detail.
Policy Issue 2 – Other technical amendments to Annex I	
Policy Issue 3 – Procedures for adapting Annex I in the future	
Policy Issue 4 – Information to the public and information management systems including reporting	
Policy Issue 5 – Land-use planning	
Policy Issue 6 – Clarifications to facilitate effective implementation	
National Regulations	
French Duty of Vigilance Law	No IA available.
Dutch Child Labour Due Diligence Law	
Italian Decree on Due Diligence	
Spanish Law on Environment and Human Rights	
Swiss Advanced Legislative Proposal	

[1316] See COMMISSION STAFF WORLING PAPER. IMPACT ASSESSMENT Accompanying document to the Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on the control of major-accident hazards involving dangerous substances. Available at: https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52010SC1590&from=EN [Accessed 11 Sep. 2019].

1.4.2 Post-Implementation Impact Assessment Review

Regarding post-implementation studies, the following table presents the main environment-related conclusions of the Environmental Liability Directive (ELD) and the EU Timber Regulation. As mentioned above, while the ELD does not involve reporting or due diligence requirements, its evaluation provides relevant criteria to consider during the refinement and designed of policy options. Moreover, the EUTR implementation evaluation confirmed the relevance of these criteria to yield positive environmental results. Nevertheless, the report states that the effectiveness of the EUTR to reduce damage caused by illegal activity is hard to quantify.

The European Commission's Report on the Implementation of the Environmental Liability Directive (2016), which establishes a framework based on the polluter pays principle to prevent and remedy environmental damage, is weakened by the fact that it is not coordinated or harmonised with the Habitats Directive. This allows for ambiguity and a fragmented interpretation of concepts such as *significant biodiversity damage* or *preventive and remedial measures* across Member States. As information is scattered and its accuracy is not clearly determined, assessing baseline conditions, determining the extent of potential impacts, and establishing causal links is very difficult. However, a key added value of the ELD is the possibility to attribute strict liability to an operator for damage to biodiversity, although, the distinction between strict liability and fault-based liability exists across different types of activities that are harmful for biodiversity. The result of this is that the procedures to prove causal links in the case of fault-base liability are exacerbated, and thus making the implementation of the ELD more complex.

In regards to the EU Timber Regulation, the 2016 evaluation indicates that the EUTR demonstrated itself to be highly relevant for tackling illegal logging and related trade by changing market behaviour patterns and freeing supply chains from illegally harvested timber. It is recognised as an important instrument to halt deforestation and forest degradation, enhance and maintain biodiversity, and address global climate change. Additionally, the report highlights the EUTR's added value of establishing uniform rules, and its coherence with other relevant policy instruments (VPAs, FLEGT AP, and the EU Wildlife Trade Regulations).

Table 8.16. Post-implementation Impact Assessments

Post-Implementation Impact Assessments/Studies	Relevant findings
EU Directive 2004/35/EC – Environmental Liability Directive[1317,1318]	
The ELD aims to establish "a framework for the prevention and remedying of environmental damage through a liability based on the 'polluter-pays principle' in order to ensure that biodiversity is restored or maintained at Favourable Conservation Status, and thus halting biodiversity loss in the EU." It requires that "operators whose activity has caused biodiversity damage or imminent threat of such damage, to be held liable."	• The ELD is not coordinated or harmonised with the Habitats Directive, leading to va *significant biodiversity damage* or *preventive and remedial measures* across Member • Information is scattered and its accuracy is not clearly determined, thus making d determine the extent of (potential) damages; establishing causal links and monitoring • A key added value of the ELD is the possibility to attribute strict liability to an opera the distinction between strict liability and fault based liability exists across differen biodiversity. The result of this is that the procedures to prove causal links in the ca and thus making the implementation of the ELD more complex.
EU Timber Regulation Implementation Reports[1319,1320]	
The EUTR "is an EU legislative instrument to address the global problem of illegal logging by acting on the side of the demand of timber and timber products." It is part of the Forest Law Enforcement Governance and Trade Action Plan (FLEGT AP), which was adopted in 2003 with the aim of improving "the supply of legal timber and to increase the demand for timber sourced from responsibly managed forests". As indicated above, the EUTR have three key obligations: (1) The placing on the market of illegally harvested timber or timber products is prohibited; (2) Operators who are placing timber and timber products on the EU market for the first time are required to exercise due diligence (risk management); (3) Traders of timber and timber products already placed on the EU market are required to keep record of their suppliers and customers (obligation of traceability).	The 2016 evaluation indicates that the EUTR demonstrated to be highly relevant for ta changing market behaviour patterns and freeing supply chains from illegally harvested instrument to halt deforestation and forest degradation, enhance and maintain biodive Additionally, the report highlights the EUTR's added value of establishing uniform rule policy instruments (VPAs, FLEGT AP, and the EU Wildlife Trade Regulations).

[1317] Milieu Ltd., IUCN (2014). Experience gained in the application of ELD biodiversity damage. Final report for the European Commission, DG Environment. [online] Brussels. Available at: https://ec.europa.eu/environment/legal/liability/pdf/Milieu%20report%20-%20ELD%20Biodiversity%20Damage.pdf [Accessed 11 Sep. 2019].
[1318] The report describes the implementation challenges of the ELD based on the analysis of 10 EU Member States environmental liability regimes. There are no pre-implementation impact assessments available for this regulation.
[1319] See COMMISSION STAFF WORKING DOCUMENT Evaluation of Regulation (EU) No 995/2010 of the European Parliament and of the Council of 20 October 2010 laying down the obligations of operators who place timber and timber products on the market (the EU Timber Regulation). Available at: https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52016SC0034&from=EN
[1320] See REPORT FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT AND THE COUNCIL Regulation (EU) No 995/2010 of the European Parliament and the Council of 20 October 2010 laying down the obligations of operators who place timber and timber products on the market (the EU Timber Regulation). Biennial report for the period March 2015 – February 2017. Available at: https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52018DC0668&from=EN

1.4.3 Benefits and Challenges of Environmental Due Diligence

Much of the literature has been developed to assess the benefits for private companies of implementing environmental safeguards. Such benefits are seen to accrue from decreasing the risks associated with lack of compliance, improving the company's image towards the general public, and even improving the company's performance. However, the literature review shows a lack of studies which aim to systematically quantify the benefits derived from environmental safeguards. The very few studies found already rely on the assumption that environmental safeguards carry positive benefits for the environment.[1321] Others indirectly state the consequences that would derive from the absence of environmental safeguards, therefore implicitly stating that these benefits (such as biodiversity protection) will happen only if environmental due diligence is set in place.[1322] Finally, another set of reports and studies makes normative statements on the benefits derived from the establishment of environmental safeguards.[1323] Only a limited number of studies made an attempt to quantify the benefits derived from these safeguards in a more systematic manner, such as the ADBs "Real-Time Evaluation of ADB's Safeguard Implementation Experience Based on Selected Case Studies", that made an economic quantification of the benefits directly derived from their program.

[1321] Annual Report on the OECD Guidelines for Multinational Enterprises 2014.
[1322] Moving towards a Common Approach to Environmental and Social Standards for UN Programming. UN Environment Management Group. Moving towards a Common Approach to Environmental and Social Standards for UN Programming (Public Draft, 2018) Accessed at https://unemg.org/wp-content/uploads/2018/11/Model_Approach_ES-Standards_30_October_2018_CONSULTATION.pdf
[1323] A Framework for Advancing Environmental and Social Sustainability in the United Nations System. UN https://sustainabledevelopment.un.org/content/documents/2738sustainabilityfinalweb-.pdf

Table 8.17: Literature on beneficial environmental impacts

Study	Benefits	Approach	Key findings	Sources
Annual Report on the OECD Guidelines for Multinational Enterprises 2014.	Environmental Safeguards benefit the environment being a tool that civil society can use to advocate for the protection of the environment by requiring for businesses to comply with certain standards	The reports shows a series of cases in which environmental safeguards served to protect the environment	There are no key findings as it the report is descriptive	OECD, 2014[1324]
Real-Time Evaluation of ADB's Safeguard Implementation Experience Based on Selected Case Studies	Based on the interpretation of changes in forest and non-forest cover from 2010 to 2015 the environmentally critical areas adjacent or traversed by the three roads experienced net increases in forest cover. Safeguard measures such as avoidance of new construction sites, planting of trees when removal cannot be avoided, and better protection by forest authorities against poachers likely contributed to the larger forest cover. Increased areas of the elephant habitats in Hurulu and Tabbowa also raise the potential number of elephants and other wildlife that could be supported.	When measuring environmental benefits the study focused on measuring the environmental safeguards on elephants as elephant constitute the country's iconic mammal for spiritual and socioeconomic reasons, however the study acknowledges that there are other environmental benefits such as forest growth.	Within the benefit calculated to be derived from environmental safeguards it was include the "value of avoided Hurulu elephant road kill" which was valued in USD 27,011 with safeguards, versus a USD 61,429 cost if there were no safeguards	Asian Development Bank, 2016[1325]
Moving towards a Common Approach to Environmental and Social Standards for	The UNEMG establishes a Model Approach to Environmental and Social Standards for UN programming and includes Biodiversity, Ecosystems and	The study does not directly quantify the benefits of environmental safeguards on the environment but it talks about the consequences in biodiversity loss that		UN Environment, 2018[1326]

[1324] OECD (2014), Annual Report on the OECD Guidelines for Multinational Enterprises 2014: Responsible Business Conduct by Sector, OECD Publishing, Paris. Available at: https://doi-org.gate3.library.lse.ac.uk/10.1787/mne-2014-en
[1325] Asian Development Bank (2016). Real-Time Evaluation of ADB's Safeguard Implementation Experience Based on Selected Case Studies. Available at: https://www.adb.org/sites/default/files/linked-documents/10-Benefits-and-Costs-of-Safeguards.pdf
[1326] UN Environment Management Group. Moving towards a Common Approach to Environmental and Social Standards for UN Programming (Public Draft, 2018) https://unemg.org/wp-content/uploads/2018/11/Model_Approach_ES-Standards_30_October_2018_CONSULTATION.pdf

UN Programming	Sustainable Natural Resource Management as one of the Thematic Areas. The document suggests that the set environmental safeguards avoid and minimize adverse impacts to terrestrial, freshwater and marine biodiversity and ecosystems.	would derive from the absence of these system of safeguards		
A Framework for Advancing Environmental and Social Sustainability in the United Nations System	Environmental Protection and Human Health	In this report it is established that the Safeguards Working Group changed the terminology from "environmental and social safeguards" to "environmental and social sustainability framework" , as the latter encompasses safeguards plus additional measures used in internal management practices and normative activities	The report establishes a series of benefit associated with the use of a common environmental and social sustainability framework which include "delivering greater environmental protection and promotion of human well-being"	United Nations, 2012[1327]
Environmental and Social Safewards System	Environmental and social safeguard standards provide guidance on how to identify risks and impacts, and are designed to help avoid, mitigate, and manage risks and impacts throughout the life of a project, and this safeguards include "Pollution Prevention and Resource Efficiency; Biodiversity Conservation and Sustainable Natural Resource Management;"	The document is mostly normative and descriptive in its approach to environmental safeguards.	Environmental safeguards have the objective to "To avoid or minimize adverse impacts on human health and the environment by avoiding or minimizing the production of wastes and pollution from project activities."	UN Habitat, 2016[1328]

[1327] UN (2012) A Framework for Advancing Environmental and Social Sustainability in the United Nations System. Available at: https://sustainabledevelopment.un.org/content/documents/2738sustainabilityfinalweb-.pdf
[1328] UN Habitat (2016) Environmental and Social Safewards System. Available at: https://unhabitat.org/un-habitat-environmental-and-social-safeguards-system/

Environmental and Social Safeguards Policy	The CEB will not knowingly finance Projects which: Are likely to cause significant and irreversible negative environmental and/or adverse social impacts.			Council of Europe Development Bank[1329]
Concept Brief Country Approaches to Safeguards	Safeguards are widely understood to be measures to protect someone or something or to prevent something undesirable; in other words, to do no harm.	Rather than key findings the UN REDD programme clarifies the role of environmental safeguards, stating that "Safeguards can build confidence and provide assurance for stakeholders that mitigation actions in the forest and land use sectors will not proceed at the expense of environmental sustainability and social equity."		UN-REDD Programme, 2016[1330]

[1329] Council of Europe Development Bank (n. d.). Environmental and Social Safeguards Policy. https://coebank.org/media/documents/Environmental_and_Social_Safeguards_Policy.pdf
[1330] UN-REDD Programme (2016). Concept Brief Country Approaches to Safeguards. Available at: https://unredd.net/index.php?option=com_docman&task=doc_download&gid=10177&Itemid=53

Despite the benefits mentioned above, studies have remained focused on the challenges that environmental safeguards pose economically and logistically both for companies and for governments. Little has been said on the current challenges that these safeguards pose for the environment, or on whether the establishment of these due diligence requirements poses any risks for the environment. The literature has however started to point to certain challenges in trying to introduce environmental safeguards. Some of the challenges found in the literature refer to the difficulties of ensuring that environmental due diligence evolves as environmental problems evolve. In this regard, it has been shown the environmental due diligence provisions of multilateral financial institutions lagged behind when trying to formally include climate change.[1331]

The rest of the literature focuses more on the challenges that arise when implementing these safeguards, given that what we refer to as the "environment" usually relates to complex systems that require from complex processes for their protection. As a result, the common challenges that arise are the lack of capacity to actually carry out these environmental due diligences as initially envisioned.[1332] More specifically, challenges such as the lack of site-specific details in environmental management plans, limited community awareness of project details, or inconsistent environmental monitoring practices, render the implementation of these safeguards more onerous than initially envisioned. Additional challenges are found in achieving regulations that do not encourage companies to seek the easier ways to comply, as indicated above in the risks presented in the pre-implementation evaluation of the mandatory due diligence option of the EU Conflict Minerals. Regarding this potential risk, similar to the findings of the human rights literature review, past research shows that the law does not restrain companies from moving business components where stricter laws do not apply or where the costs of complying are lower. Nevertheless, the literature also identifies potential benefits that may counterbalance this negative effects, such as the development of sustainable business-models[1333], which in the long-term may be helpful to improve conditions in the new locations.

Table 8.18: Literature on challenges to existing environmental due diligence

Study	Challenges	Key findings	Sources
Approaching climate adjusted environmental due diligence for multilateral financial institutions	Although environmental safeguards continue to play vital roles in bank operations, it generally remains traditional with minimal adjustments to formally include climate change	This study looks into literature on environmental safeguards for five selected multilateral financial institutions (MFIs) with the objective of verifying whether their environmental safeguards have been updated with climate change elements, and whether they have adopted specific climate change strategies for their investment portfolios, and finds that minimal adjustments have been	Kwame Boakye-Agyei,2011[1334]

[1331] Boakye-Agyei, K. (2011). Approaching climate adjusted environmental due diligence for multilateral financial institutions. International Journal of Climate Change Strategies and Management, 3(3), 264-274. doi:http://dx.doi.org.gate3.library.lse
[1332] Asian Development Bank. RETA 7548: Improving of Environmental Safeguards in Central and West Asia, Georgia Country Report. Accessed at https://www.adb.org/sites/default/files/project-document/42973/43333-012-tacr-03.pdf
[1333] Clark, Gordon L. and Feiner, Andreas and Viehs, Michael (2015). From the Stockholder to the Stakeholder: How Sustainability Can Drive Financial Outperformance. Available at SSRN: https://ssrn.com/abstract=2508281
[1334] Kwame Boakye-Agyei, (2011) "Approaching climate adjusted environmental due diligence for multilateral financial institutions", International Journal of Climate Change Strategies and Management, Vol. 3 Issue: 3, pp.264-274, https://doi.org/10.1108/17568691111153410

		made to formally include climate change.	
Improving the Implementation of Environmental Safeguards in Central and West Asia	Insufficient capacity in executing agencies to prepare, implement, and monitor the implementation of EMPs.	Amongst other issues this report points out towards the challenges that arise when trying to implement ambitious environmental safeguards when the institutional capacity to do so is limited	Asian Development Bank, 2014[1335]
Assessing the impact of institutional conditions upon REDD+	The introduction of complicated systems of safeguards have all affected the emergence of 'pure' REDD+ in Guyana.	The basic theoretical approach of certain natural resources management programs (such as REDD+) can be hampered by the imposition of certain environmental safeguards	Laing, Timothy, 2014[1336]
Assessing the impact of institutional conditions upon REDD+	Challenges arise when balancing policy freedom and environmental safeguards.	Finding the right balance between policy freedom and sufficient safeguards will be crucial for producing JNR that is both effective and equitable.	Laing, Timothy, 2014[1337]
Safeguard Implementation: How can we make it more meaningful?	Ongoing challenges in coordinating safeguard responsibilities and monitoring between institutions and resident missions (lack of human resources and time to undertake the required field missions; lack of timely computer based reporting of safeguard status; different stages of the safeguard process are handled by different people; and lack of clarity in the headquarters–resident mission handover process, when projects are delegated to the resident missions).	By looking carefully at safeguard measures that are exemplary and working effectively in each country, and examining the context and dynamics that contribute to their effectiveness, the study tries to understand how to rectify safeguard measures that are lagging. Amongst other challenges, the study identifies the following challenges and shortcomings: • Lack of site-specific details in environmental management plans • Lack of community awareness of project details • Absence of a role for Local Communities in Mitigation and Monitoring • Inadequate Implementation of Environmental Management Plan • Inconsistent Environmental Monitoring.	Asian Development Bank, 2015[1338].

[1335] Asian Development Bank, (2014). RETA 7548: Improving of Environmental Safeguards in Central and West Asia. Georgia Country Report. Accessed at https://www.adb.org/sites/default/files/project-document/42973/43333-012-tacr-03.pdf
[1336] Laing, Timothy (2014) Assessing the impact of institutional conditions upon REDD+. PhD thesis, The London School of Economics and Political Science (LSE). http://etheses.lse.ac.uk/1024/1/Liang_Assessing_the_impact_of_institutional.pdf
[1337] Laing, Timothy (2014) Assessing the impact of institutional conditions upon REDD+. PhD thesis, The London School of Economics and Political Science (LSE). http://etheses.lse.ac.uk/1024/1/Liang_Assessing_the_impact_of_institutional.pdf
[1338] Asian Development Bank, (2015). Safeguard Implementation: How can we make it more meaningful? Accessed at: https://www.aecen.org/sites/default/files/safeguard-implementation_1.pdf

1.5 Impact on Public Authorities

Potential impacts on the public administration at the EU level as well as Member State level and the legal systems have been assessed in previous impact assessments of similar legislation.

In the EU's impact assessment on the Non-Financial Reporting Directive[1339], the assessment concludes that the proposed measures will not have any meaningful consequences for the budget of public authorities in Member States or the EU budget. Although the Commission will monitor the implementation of the Directives in cooperation with the Member States throughout the implementation period, it is expected that the cost for such monitoring activities "would be met from existing operational budgets, and would not be significant." The monitoring is expected to include sample reviews of non-financial statements or reports. A possible cost impact is expected from data collection activities at EU level, but it is expected to be low as these activities would use existing structures and instruments. The impact assessment also considers the possibility to conduct an external study on the implementation of the new reporting obligation and its effects.

In contrast, the EU's impact assessment on the Conflict Minerals Regulation[1340] (for a detailed description of the EUTR, please see

Table 8.2) provides detailed cost estimates for the expected administrative costs for the European Commission and EU Member States (MS). The Conflict Minerals Regulation requires oversight or enforcement of compliance at Member State level. According to the impact assessment, some of these estimates are "based on information derived from experiences under the EU Timber Regulation"[1341], which also provides for a degree of oversight by Member States. An overview of the expected economic costs for each of the considered legislative options and the related compliance control mechanisms is provided in Table 8.19 below. Most costs are provided in terms of a "full-time equivalent (FTE)", which is equivalent to one employed person working on a full-time schedule.[1342]

[1339] See COMMISSION STAFF WORKING DOCUMENT IMPACT ASSESSMENT Accompanying the document Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL amending Council Directives 78/660/EEC and 83/349/EEC as regards disclosure of non-financial and diversity information by certain large companies and groups. Available at https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52013SC0127.

[1340] See European Commission (2014), Impact Assessment Accompanying the document Proposal for a Regulation of the European Parliament and of the Council setting up a Union system for supply chain due diligence self-certification of responsible importers of tin, tantalum and tungsten, their ores, and gold originating in conflict-affected and high-risk areas. PART 1 (Impact Assessment). Retrieved from: https://eur-lex.europa.eu/legal-content/EN/TXT/DOC/?uri=CELEX:52014SC0053&from=EN.

[1341] See European Commission (2014), Impact Assessment Accompanying the document Proposal for a Regulation of the European Parliament and of the Council setting up a Union system for supply chain due diligence self-certification of responsible importers of tin, tantalum and tungsten, their ores, and gold originating in conflict-affected and high-risk areas. PART 1 (Impact Assessment), page 50.

[1342] The unit is obtained by comparing an employee's average number of hours worked to the average number of hours of a full-time worker. Eurostat.

Table 8.19: Estimated economic cost for EU and MS public authorities from the EU Conflict Minerals Regulation

Regulatory Option	Administrative burden
Option 1 – Standalone EU communication & Option 2 – Soft Law	• Promotion via National Contact Points and the Enterprise Europe Network: 0.05 FTE • Financial assistance to the OECD due diligence action: €0.2 million annually over 5 years • Due diligence requirements relating to EC public procurement contracts for IT hardware: additional cost of maximum 7,000 EUR per annum • Drafting of public procurement guidance and further outreach by EC: 1 FTE • Voluntary uptake of due diligence requirements by Member States' public authorities: 18% of GDP in the EU, which is 420 billion EUR, is used for public procurement to which a maximum of 0.014% cost increase would apply to procurement contracts in the relevant sectors
Option 3 – Regulation establishing obligations under an "EU responsible Importer" certification based on the OECD Guidance – VOLUNTARY	• Taking care of implementing guidance at EC: 1.5 FTEs • One external study on the implementing guidance: 200,000 EUR • Cost of management committee meetings twice a year with Member States: 60,000 EUR • In each of the EU Member States, the scheme would require 1 FTE in designated control bodies for coordination of ex-post compliance controls and inspections
Option 4 - Regulation establishing obligations under an "EU responsible importer" certification based on the OECD Guidance – MANDATORY	• Implementing guidance at EC: 2 FTEs • One external study on the implementing guidance: 200,000 EUR • Cost of management committee meetings four times a year with Member States: 120,000 EUR • In each of the EU Member States, the scheme would require 1.5 FTEs in designated control bodies for coordination of ex-post compliance controls and inspections
Option 5: Directive establishing obligations for EU-listed companies based on the OECD Guidance	• Implementing guidance at EC: 2 FTEs • One external study on the implementing guidance: 300,000 EUR • In each of the EU Member States, the scheme would require 2 FTEs in designated control bodies for coordination of ex-post compliance controls and inspections
Option 6 – Prohibition of imports when EU importers of ores fail to demonstrate compliance with the OECD Guidance – import ban	• Negotiation of an international agreement and implementing guidance at EC: 3 FTEs • Outreach towards third countries: 1 FTE • One external study on the implementing guidance: 300,000 EUR • Cost of management committee meetings four times a year with Member States: 120,000 EUR • Cost of handling stockpiled shipped goods that had been refused at entry, but difficult to quantify • In each of the EU Member States, the scheme would require 1.5 FTEs in designated control bodies for coordination of ex-post compliance controls and inspections, and handling of stockpiled shipped goods that had been refused entry.

These two impact assessments are considered to provide the best most useful assessments of impacts on public administration since they provide a discussion or cost estimates for activities, which may also be carried out under a new due diligence regulation.

The EU Impact Assessment on the Timber Regulation[1343] also provides estimates for "regulatory cost", which is considered to be the cost incurred by government. However, the activities, for which cost estimates have been provided, are less representative for possible expected activities under a new regulation than the estimates provided in the EU Conflict Minerals Impact Assessment. The assessed activities in the related impact assessment consist, for example, of the checking of samples of timber consignments which have been imported or originate from EU Member States concerning the legality of the product (regulatory options 3 and 4B). For regulatory option 4A (Legislation which prohibits the trading and possession of timber and timber products harvested in breach of the laws of the country of origin) the impact assessment considers regulatory costs "related to investigations conducted by the EU police force or other enforcement authorities". However, but it does not provide any estimates as it states that "the total costs for such investigations are difficult to assess and depend on the number of cases identified and ultimately prosecuted". For regulatory option 5 (Legislation requiring companies placing timber on the market to exercise due diligence in ascertaining that the products are legal), the impact assessment expects regulatory costs from the "verification whether effective systems have been put in place by operators for ascertaining that the products are legal" and estimates regulatory costs in the EU of 1 million EUR per year.

For the EU Timber Regulation[1344] (EUTR) the latest biennial implementation report[1345] was reviewed together with the related background analysis.[1346] The background analysis report provides the more detailed analysis and the biennial implementation report basically summarises the findings from the background analysis. There are also "national reports" available on the website, but these contain only the reporting forms for each MS which they had to fill out. All results from these reporting sheets are provided also in overview tables in the background analysis report and in a shortened form in the implementation report.

The background analysis of the 2015-2017 national biennial reports synthesises the biennial reports on the application of the EUTR by EU Member States and Norway over the period March 2015 to February 2017. The report provides the results from all received national reporting forms for different areas such as the existence of national legislation for the implementation of the EUTR, implementation and enforcement, cooperation activities on the implementation and enforcement, technical assistance and capacity development and communication activities by MS as well as the resources needed by the competent authorities. The report provides a quantitative assessment for

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[1343] European Commission (n.a.). Staff Working Document. Accompanying document to the Proposal for a Regulation of the European Parliament and of the Council determining the obligations of operators who make timber and timber products available on the Market. Impact Assessment. Retrieved from: https://ec.europa.eu/environment/forests/pdf/impact_assessment.pdf
[1344] See: https://ec.europa.eu/environment/forests/eutr_report.htm
[1345] European Commission (2018). Evaluation of Regulation (EU) No 995/2010 of the European Parliament and of the Council of 20 October 2010 laying down the obligations of operators who place timber and timber products on the market (the EU Timber Regulation). Retrieved from: https://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1538746572677&uri=COM:2018:668:FIN.
[1346] European Commission (2018). Background analysis of the 2015-2017 national biennial reports on the implementation of the European Union's Timber Regulation (Regulation EU No 995/2010). Retrieved from: https://ec.europa.eu/environment/forests/pdf/WCMC%20EUTR%20analysis%202017.pdf

the latter, but the quality and comparability of the reported data by Member States remains relatively low, which makes it difficult to draw general conclusions from the provided information.

The implementation and enforcement of the EUTR is to be carried out by "Competent Authorities" in Member States. According to the background analysis report, all Member States[1347] confirmed that they have designated a Competent Authority to monitor whether the implementation of the EUTR by operators is in line with the requirements of the Regulation. The institutional structures, legal powers and status of the designated authorities vary between Member States, due to their different legal and institutional frameworks. The Competent Authorities are usually state agencies, ministries or ministerial departments for forest, environment or agriculture.

Member States also report on their national penalties applicable to infringements of the EUTR. 13 countries stated that both administrative and criminal penalties could be imposed, 10 confirmed that administrative penalties were possible, and 2 stated that criminal penalties could be imposed.

The Competent Authorities in each country are required to put in place a plan for checks of operators and procedures for checks on Monitoring Organisations to verify their compliance with the EUTR. The more detailed tasks carried out by the Competent Authorities are described in the background analysis as follows: Checks on operators and traders, checks on Monitoring Organisations[1348], the provision of guidance as well as technical and other assistance to operators[1349] to facilitate compliance with the EUTR (particularly relating to the implementation of the due diligence requirement) and communication to convey information about the EUTR to stakeholders.

Apart from reporting on their tasks, Member States also had to report on their human and financial resources which they have available for their Competent Authorities to carry out the required tasks. However, as stated above, the report emphasizes that "the majority of the figures included in this section are difficult to compare due to the varying levels of detail provided by countries in their national reports." In addition, the human and financial resources of the Competent Authorities varied greatly across the responding countries.

Concerning human resources, the background analysis report describes that for timber imported into the EU, available human resources of Competent Authorities ranged from 0.125 full time equivalent (FTE) staff to as many as 10 staff (in the official biennial implementation report the upper estimation is 8 staff which seems to be the correct figure). Similarly, for domestic timber, available human resources varied between 0.125 FTE and 20 staff. For both estimates, i.e. for imported as well as domestic timber estimates, the relatively high number of human resources reported by Italy, Greece, Denmark and Bulgaria were taken as outliers and removed from the report.[1350] In

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[1347] All 28 EU Member States submitted biennial reports on their implementation of the EU Timber Regulation (EUTR). The report also includes information on the application of the EUTR in Norway as a member of the European Economic Area (EEA).
[1348] There are 13 Monitoring Organisations12 established in the EU, many of which also offering their services in countries where they do not have an office. The main offices of Monitoring Organisations should be checked by the Competent Authority of this country every 2 years, and Competent Authorities should also regularly check Monitoring Organisations that do not have their main seat in their country but are offering their services there.
[1349] Twenty-three (23) countries provided details of assistance and training provided to operators by government organisations. The most frequently reported method of assistance was lectures or seminars (10 countries) followed by the provision of information on the website of the organisation in question (8 countries).
[1350] The report states that the "relatively high number of human resources reported by Italy, Greece, Denmark and possibly others may be based on customs personnel or other supporting staff in general also having been included."

addition, in many countries the core staff are also supported by others, who are not primarily focused on EUTR implementation and enforcement (e.g. forest inspectors).

In relation to financial resources, some countries have reported extremely limited budgets for implementation and enforcement of the EUTR (e.g. Belgium), whereas others (e.g. Germany) reported that they did not have an upper limit.

The detailed information provided by each country is presented in the two overview tables below. However, it is important to emphasize that these figures relate to reported current human and financial resources of Competent Authorities rather than the required financial and human resources.

Table 8.20 Human resources available for the implementation and enforcement of the EUTR as reported in the background synthesis report (FT: full time equivalent staff, PT: part time equivalent staff)

Country	Imported timber	Domestic timber
Austria	2.5 (2 953.5 working hours)	20 person months
Belgium	0.5 FT	0.5 FT (shared with imported timber, not used in 2016)
Bulgaria	20	20
Croatia	1	1
Cyprus	2 PT (60-70% of time)	22 PT (30-40% of time)
Czech Republic	39 PT	39 PT
Denmark	24	24
Estonia	1 FT*, with assistance as required	11 FT
Finland	1 FT and 2 PT	1 FT and 2 PT
France	6.3 FT	6.3 FT
Germany	~ 10 FT (only CA)	several PT for each administrative region (16)*
Greece	45	68
Hungary	8	8
Ireland	4	4
Italy	90	2400

Latvia	1	1 FT**
Lithuania	1 FT, with assistance from 11 regional specialists	1 FT
Luxembourg	0.125	0.125
Malta	1	N/A
Netherlands	3	3 (including imported timber)
Norway	1 PT (43% of time)	1 part time (~17%)*
Poland	7	7
Portugal	CA: 1 FT*, 1 PT (~65% of time)*; Regional CA:12 PT (10% of time); Azores: 1 FT*, 11 PT (10% of time), 8 forest guards; Madeira: 1 FT*, 2 PT (10% of time)	Resources shared for domestic and imported timber
Romania	Not specified	Not specified
Slovakia	Not specified	Not specified
Slovenia	2 FT	14 PT
Spain	24 PT in March 2015; 42 PT in February 2017	24 PT in March 2015; 42 PT in February 2017
Sweden	~ 2.2 FT	~ 0.3 FT
United Kingdom	5 FT**	Resources shared for domestic and imported timber

**Due to limited levels of detail provided, this information was inferred.*

***Core staff also supported by other human resources.*

The second relevant set of assessments is the 2016 evaluation of the EUTR.[1351] In this evaluation, the public sector costs created for Member States are described, but only in a qualitative and general form: "The resources allocated by the Member States for monitoring the application and enforcement of the Regulation depend on the size of the country and its institutional structure and governance, the characteristics of the forest sector, including land tenure and traditional management systems, as well as legality risks involved."

Furthermore, the evaluation report finds that small countries have lower allocations of resources than larger ones, but also states that the pattern of government expenditures includes variations that cannot be explained by the size of the forest sector alone.

Regarding the human resources indicated by the reporting Member States (23 Member States included this information in their biennial reports), the evaluation report finds that these range approximately from 1 to 200 persons-month per year.

Regarding the financial resources indicated by the reporting Member States (only 9 Member States provided quantitative information on their financial expenditure), the evaluation report finds that these vary approximately between EUR 10 000 to EUR 370 000 per year for monitoring the application of the EUTR, including information-sharing activities and enforcement.

The Seveso III Directive (2012/18/EU)[1352] aims at the prevention of major accidents involving dangerous substances as well as at limiting the consequences of such accidents for human health and the environment. The Directive requires Member States to ensure that operators fulfil several obligations, including, for example, producing external emergency plans for high-risk establishments, deploying land-use planning for the siting of establishments, making relevant information publicly available, or conducting inspections. The latest Commission report available on the website, i.e. the Report on the Application in the Member States of Directive 96/82/EC on the control of major-accident hazards involving dangerous substances for the period 2009-2011, does not provide any information on the costs incurred by the competent authorities. The Impact Assessment[1353] of the Seveso III Directive discusses mainly costs for operators, but also considers some costs for competent authorities. However, some of the costs refer to changes of an existing Directive (e.g. technical changes to the Annex I) and can therefore not be applied to the assessment of a completely new regulation. This is the case for the costs for authorities estimated for policy issues 1 to 3, which refer to changes of Annex I. These options have a cost impact regarding the scope of the Directive, meaning that the number of affected companies would change (new companies would be subject and companies subject to the requirements previously would fall out of the scope of the requirements). The adjustment costs for authorities are estimated from around 400,000 EUR (policy issue 1) to 800,000 EUR (policy issue 3) per year for the competent authorities.

[1351] European Commission (2016). Evaluation of Regulation (EU) No 995/2010 of the European Parliament and of the Council of 20 October 2010 laying down the obligations of operators who place timber and timber products on the market (the EU Timber Regulation). Retrieved from: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52016SC0034.
[1352] For more information, please see: European Commission (2019). Major accident hazards. Available at: https://ec.europa.eu/environment/seveso/legislation.htm.
[1353] See European Commission (2010). COMMISSION STAFF WORKING PAPER IMPACT ASSESSMENT Accompanying document to the Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on the control of major-accident hazards involving dangerous substances. Retrieved from: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52010SC1590.

Under policy issue 4 (Information to the public and information management systems including reporting), the impact assessment provides estimates for the provision of different types of information to the public and in different forms as described in the table below. For policy option 5 (Land-use planning) the Impact Assessment provides cost estimates for some on-site assessments of establishments by the competent authorities.

Table 8.21 Estimated costs for authorities in the Seveso III Impact Assessment

Regulatory Option	Impact on public authorities
Policy issue 4: Information to the public and information management systems including reporting	**Costs estimates for type of information provided** • To make existing information (Annex V) available on existing governmental websites (policy issue 4) it is estimated that the total one-off costs for authorities would be about 1 million EUR. • For a more comprehensive provision of information (e.g. basic data on establishments and on main type of major accident scenarios) the Impact Assessment estimates total one-off costs of 2-4 million EUR with an annual cost of updating the information of about 0.5 million EUR. • If the provided information would be even more comprehensive and also include addition non-technical summaries of the key documents, the safety report and the external emergency plans to be made publicly available, the total one-off cost for competent authorities is estimated at the order of EUR 3 to 4 million (assuming that no such documents are currently produced). The cost for updating the information every three years is estimated at an average total annual cost of around EUR 2-5 million. **Cost estimates for different types of information management** • A system in each Member States which includes a simple website structure and basic tasks such as uploading relevant documents and information for each establishment is estimated at a total one-off cost of about 1 million EUR. • A central EU website that can be used to access information in all Member States either through links to documents directly uploaded on to it or links to Member State websites/databases which would use existing IT infrastructure and existing databases is estimated to cause total set-up costs of around 0.5 to 1million EUR. The operation and maintenance costs would be about 50,000 to 100,000 EUR per year. • The cost for a centralised EU database with all information integrated which would require Member States adapting their existing systems cannot be estimated without a detailed analysis of the system requirements, but are likely to be very substantial.
Policy issue 5: Land-use planning	• The cost for competent authorities to make an in-depth site-by-site analysis of the situation to assess whether or not there are appropriate safety distances and to identify what remedial land-use measures might be needed is estimated at a total cost of more than EUR 130 million.

The EU Environmental Liability Directive (ELD, Directive 2004/35/EC)[1354] establishes a framework based on the polluter pays principle to prevent and remedy environmental damage. No official impact assessment was found online, but a report on the implementation of the ELD.[1355] The report, however, concludes that it is not possible to draw sound conclusions on the administrative costs because of the limited information on administrative costs for authorities. It states that only three Member States (Belgium, Bulgaria, and Spain) provided precise data on administrative costs for public authorities, which vary considerably. The reported costs range from EUR 55,000 per year (in the Flemish Region of Belgium) to annual administrative costs of EUR 135,613 per year in Bulgaria and EUR 2 million (in some of the autonomous communities of Spain). At a later stage the report again refers to administrative costs and states that "no comparable figures exist". It then provides examples for reported administrative costs from some Member States as described below. However, as the report states, it is not clear how these costs are estimated, to what they refer and what they include and they do not seem to be comparable:

- Belgium indicated that they have not seen additional administrative costs at federal State level and Hungary communicated that no additional administrative costs were incurred by the public administration.
- Greece reported about one newly created authority at central level as well as fourteen supporting Committees, for the purpose of the implementation of environmental liability.
- Ireland indicated running costs of one person per year.
- Italy indicated in qualitative terms a "high amount of necessary human and technical resources".
- The United Kingdom reported an "educated guess" in the region of 15 full time equivalent staff years in relation to the preparation of the transposing legislation, supporting guidance, staff training and communication activities while ongoing implementation costs are relatively modest.

The EU Directive on the protection of the environment through criminal law, called Environmental Crime Directive (ECD) (Directive 2008/99/EC), lays down a list of environmental offences that must be considered criminal offences by all Member States. The Directive requires EU Member States to attach to the existing prohibitions criminal sanctions and that legal persons can be held liable for offences committed for their benefit. This responsibility can be of criminal or other nature. However, the directive does not lay down measures concerning the procedural part of criminal law nor does it touch upon the powers of prosecutors and judges.[1356]

[1354] For more information, please see: European Commission (2019). Environmental Liability. Retrieved from: https://ec.europa.eu/environment/legal/liability/index.htm.
[1355] Brussels, 14.4.2016 COM(2016) 204 final REPORT FROM THE COMMISSION TO THE COUNCIL AND THE EUROPEAN PARLIAMENT Report from the Commission to the Council and the European Parliament under Article 18(2) of Directive 2004/35/EC on environmental liability with regard to the prevention and remedying of environmental damage. Retrieved from: https://ec.europa.eu/transparency/regdoc/rep/1/2016/EN/1-2016-204-EN-F1-1.PDF.
And COMMISSION STAFF WORKING DOCUMENT REFIT Evaluation of the Environmental Liability Directive Accompanying the document Report from the Commission to the European Parliament and to the Council pursuant to Article 18(2) of Directive 2004/35/EC on environmental liability with regard to the prevention and remedying of environmental damage. SWD/2016/0121 final. Retrieved from: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=SWD:2016:121:FIN.
[1356] For more information see European Commission (2019). Combating Environmental Crime. Available at: https://ec.europa.eu/environment/legal/crime/index.htm.

The Impact Assessment[1357] for this Directive remains generally very vague and primarily assesses the possible impacts in terms of "slight" and "strong" positive or negative impacts. The possible impacts on public authorities are described very generally and no quantification of costs is provided. The information on impacts on public authorities for the two main policy options is described in the table below. Policy option 2, which aims to encourage cooperation among MS on a voluntary basis, would consist of the Commission organizing workshops or meetings of relevant authorities in the Member States to exchange knowledge on the different environmental crime laws in order to initiate and improve cooperation between Member States in the fight against environmental crime. Under policy option 3, the Commission would present a proposal for legislation on the protection of the environment through criminal law. This would oblige MS to accept certain goals but allow for flexibility regarding the implementation into their national laws and the right to take or keep measures that go beyond the proposed EC standard.

Table 8.22 Estimated impacts on public authorities in the Impact Assessment of the EU Directive on the protection of the environment through criminal law

Regulatory Option	Impact on public authorities
Policy Option 2: Encourage cooperation between Member States	• Awareness-raising activities conducted by the Commission on a voluntary basis would only involve very limited costs for public authorities • Benefit would be the improvement of contacts between public authorities from different Member States • Not expected to lead to big changes to the differences in criminal sanctions throughout the Community
Policy Option 3: Set minimum regulatory standards	• Potentially higher costs of more criminal proceedings in some MS • Possible is also the contrary, i.e. fewer proceedings because of deterrent effect

A review was carried out by EFFACE (European Union Action to Fight Environmental Crime), a 40-month EU funded research project. The objective was to assess the impacts of environmental crime as well as effective and feasible policy options for combating it from an interdisciplinary perspective, with a focus on the EU. The project ended in March 2016.The final synthesis[1358] report concluded that one of the main challenges was data and information management in the area of environmental crime. Concerning the potential impacts for public authorities it reports that "Information on the sanctions effectively imposed by the judiciary is also lacking. Such information is often not collected in a consistent way by Member States; as a consequence, no reliable or comprehensive data is available for the EU, either. If that type of information is lacking, it becomes very difficult to judge to what extent criminal enforcement can be considered as 'effective, proportionate and dissuasive' as required by the ECD."

[1357] European Commission (2007). COMMISSION STAFF WORKING DOCUMENT Accompanying document to the Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL
on the protection of the environment through criminal law IMPACT ASSESSMENT. Retrieved from: https://ec.europa.eu/smart-regulation/impact/ia_carried_out/docs/ia_2007/sec_2007_0160_en.pdf.
[1358] European Union Action to Fight Environmental Crime (2016). ENVIRONMENTAL CRIME AND THE EU - Synthesis of the Research Project "European Union Action to Fight Environmental Crime" (EFFACE). Retrieved from: efface.eu/sites/default/files/publications/EFFACE_synthesis-report_final_online.pdf.

When discussing the system of sanctions, the report mentions as "one weakness of the system of sanctions, which is being defined by Member States in the absence of harmonized EU rules on the matter, is that the mix of sanctions (administrative/criminal/civil) at Member State level is not always optimal. While some Member States do have possibilities for administrative authorities to impose specific measures, in others these powers seem either to be missing or are rarely applied. […] The same is true concerning the system of administrative fines." The report then provides an overview and comparison of the different types of approaches and sanctions to addressing environmental crime. As part of this overview it also briefly describes and compares the expected cost for the state arising from the different systems (see Table below), but it does not provide any cost estimates.

Table 8.23 Expected costs for public authorities from criminal, administrative and civil law approaches to addressing environmental crime in EFFACE synthesis report

Criminal law approach	Administrative approach[1359]	Civil law suits
Costs of proceedings born mostly by state; relatively high costs for the state due, among others, to high threshold of proof and length/complexity of proceedings	Typically, lower costs for the state than in criminal proceedings, among others because of less complex proceedings	Relatively low costs for the state, but often high costs for the parties, as they are responsible for producing evidence

2. Methodology

2.1 Economic and Social Impact Assessment

The economic and social impacts assessment of regulatory options covers the following subjects:

- Company-level impacts (costs and benefits)
- Sector- and economy-wide impacts (costs and benefits)
- Social impacts in the EU and non-EU countries with a particular focus on employment and employment conditions
- Impacts on the public authorities in the EU's Member States (costs)

2.1.1 Economic Impacts: Company-level, sector- and economy wide impacts

For company-level as well as sector- and economy-wide impacts, we outline impacts related to the additional cost burden on the basis of the proposed options, potential commercial benefits resulting from the proposed measures and analyse their implications for competitiveness, international trade relationships and the innovative capacities of European businesses.

We start with a detailed evaluation of the survey responses, particularly with respect to the cost estimates and respondents' statements regarding the potential commercial

[1359] "Regarding terminology, it should be noted that what is referred to as administrative sanction or measure in most countries, may be a called a "civil sanction" or similar in common law systems like in the UK."

benefits. Due to the large amount of data, we restructure the data to identify patterns and differences in the potential impacts between large companies and SMEs and variations between different sectors of the economy. We also perform a sanity check of the information given by the respondents to identify and correct for inconsistencies.

Costs

Company-level: Based on the survey results, we take into consideration estimations for DD-related costs. We consider for estimates from companies with no experiences in DD activities as well as companies' that already undertake DD activities, i.e. current DD practices and the costs associated to these activities. For different groups of companies (large companies vs. SMEs; experienced vs. non-experienced), we quantify the differences in costs for each of the proposed policy options. To account for potential economies of scale, the quantification of both absolute costs and relative increases in costs is based on companies' size (by number of employees) and annual sales levels. The resulting estimates are checked against the findings of related literature, particularly previous impact assessments of related policies, e.g. the EU and US conflict minerals regulations, the EU Timber Regulation, and the EU Non-financial Reporting Directive.

Sector-level: We calculate sector-specific impacts on the basis of the estimates gathered from the survey respondents' and estimates provided by additional literature. Based on the discussion with the client, we provide cost estimates for EU companies that operate in mining and extraction industries, textile industries and companies trading and manufacturing food products and agricultural commodities. To determine sector-specific cost impacts, the company-level cost estimates are extrapolated on the basis of data from the EU's business demography database, which provides statistics for a wide range of economic activities, including the number of companies by sector and revenue data.[1360]

Economy-level: The results of the sector-level analysis are extrapolated for the estimation of an EU economy-wide impact.

SMEs: Specific attention is paid to SMEs. We link the company-level estimates for SMEs to data from the EU's Structural Business Statistics for SMEs, which provides annual enterprise statistics for SME activities by size class for all sectors of the economy.[1361]

Impact on innovation and long-term competitiveness: The analysis of the impact on innovation and long-term competitiveness of EU businesses is based on the proceeding cost-benefit analysis and literature on the impact of regulation on innovation.[1362] The discussion is largely qualitative by nature as the determinants of innovation are numerous and difficult to disentangle.

Use of new technologies: we discuss how the use of new (digital) technologies can contribute to cost savings regarding the implementation of DD policies.

Benefits

1360 Database on Structural Business Statistics and Global Business Activities. Available at https://ec.europa.eu/eurostat/web/structural-business-statistics/entrepreneurship/business-demography.

[1361] Database on Structural Business Statistics for Small- and Medium-sized enterprises. Available at https://ec.europa.eu/eurostat/web/structural-business-statistics/structural-business-statistics/sme.

[1362] See, e.g., Blind, K. (2012). The Impact of Regulation on Innovation. Nesta Working Paper No. 12/02. Available at https://pdfs.semanticscholar.org/5877/b0b479ac929d776c6b2212295b2e5450de22.pdf.

Company-level: Potential economic benefits, which may arise from the different policy options, are discussed based on the survey results and complemented by findings from the literature. The survey respondents' ratings regarding different types of benefits for each regulatory option are presented and discussed for each policy option. Where literature findings could be associated with the assessed policy option these were discussed in relation to the respective policy option.

Sector-level: Depending on the availability of relevant information, we consider the literature as well as survey replies to derive sector-level impacts, which are discussed qualitatively.

SMEs: Where possible, the discussion of benefits also pays specific attention to SMEs. Based on the differences in the survey responses that can be attributed to differences in firm size, we provide a discussion of the benefits in the context of the findings regarding the main activities and sectors of EU SMEs.

2.1.2 Social Impacts in the EU and non-EU countries

The analysis of the social impact largely focuses on the impact of the proposed policy options on employment and working conditions in the EU and non-EU countries. We take into consideration potential positive and negative impacts which may arise under the different policy options and briefly discuss potential adverse impacts in third countries. The analysis is mainly qualitative. Based on the estimates derived in the firm level assessment, we provide estimations about potential employment effects for the EU.

2.1.3 Impacts on the public authorities in EU Member States

We provide a discussion of the administrative burden for EU Member States' authorities as well as potential benefits for each policy option. This analysis is informed by reports on the costs of law enforcement for related policies in different Member States and include the findings from related impact assessments.

2.2 Human Rights and Environmental Impact Assessment

The human rights and environmental impact assessment covers the following subjects:

- Environmental impacts, including impacts on climate, resource efficiency and biodiversity;
- Impact on fundamental rights obligations and international commitments, focused in particular on children and other vulnerable communities.

2.2.1 Impacts on Human Rights

For the human rights impacts assessment, we outline impacts arising from due diligence mechanisms related to:

- Obligations and international commitments (supply-side of human rights)
- Ability of rights-holders to demand duties be met; (demand-side of human rights)
- Impacts on children and vulnerable communities

While the original project objectives included an issue-specific analysis of policy options regarding the rights of the child and child labour within agricultural supply chains, it was expressed by stakeholders that the analysis should be cross-sectoral. As such, DG Just and the research team prioritized a cross-sectoral methodology and expressly excluded issue specific options from the scope of the mandate.

An in-depth review of the survey responses particularly focuses on respondent's expectations of the ability of the four policy options to have an impact on human rights. Distinguishing between stakeholder estimations and self-reported expectations from business representatives, the estimated impacts on specific human rights is assessed.

Potential increases in both the supply-side and demand-side of human rights which may arise from the different policy options are explored employing survey results as well as evidence from existing literature. As respondents were asked to provide expected impacts that may arise from each policy option, the analysis can benefit from both an analysis of each option across sectors and across human rights obligations and international commitments. The varying expected levels of impact are assessed for a preliminary assessment of the capacity of each policy option to further meet obligations and international commitments.

2.2.2 Environmental Impacts

For the environmental impacts assessment, we outline impacts arising from the due diligence mechanisms related to:

- meeting international standards;
- potential effects on the climate;
- resource efficiency;
- and biodiversity

The analysis begins with an in-depth review of the survey responses, paying specific attention to the respondent's expectations of the various due diligence options' ability to have an impact on the environment. Thereafter, the estimated impacts within specific areas of environmental sustainability are assessed, particularly differentiating between stakeholder perceptions and self-reported impacts along companies' supply chains. The analysis ensures to review geographical areas of operation and current realities. Finally, the analysis as much as possible links results from the economic impacts analysis for a discussion on a sector's expectation to decrease environmental impacts via due diligence requirements and faced costs to arrive at an understanding of the realistic possibilities of the changes.

To assess impacts on climate change mitigation, we assess companies' current due diligence practices and the self-reported survey results from their expected impacts of new due diligence regulations. Considering the wide range of industry representation, the analysis takes into account the varying levels of possible contribution to climate change – for example in recognition that some sectors such as manufacturing, mining, agriculture, and transport may have greater impacts than others, such as education. Findings are cross-checked against relevant literature where possible.

Potential increases in resource efficiency which may arise from the different policy options is explored employing survey results as well as evidence from existing literature. As respondents were asked to provide the level of expected impact (not significant – very significant) that may arise from each policy option, the analysis can benefit from both an analysis of each option and across sectors. As already noted, the study takes into account that some sectors may have a greater capacity to increase resource efficiency due to already larger existing environmental impacts because of the nature of the industry itself.

3. Analysis

The following section sets out the preliminary analysis for the assessment of regulatory options. It is based on and draws from the literature review, the assessment of the survey results, and the findings from the Market Practices and Regulatory Review sections. The impact assessment combines quantitative and qualitative approaches as far as possible and aims to discuss and assess possible costs and benefits of the different policy options in the following areas: economic impacts, social impacts, environmental impacts, impacts on human rights, and impacts on public authorities in the EU. Due to the differing approaches and conceptual elements between the economic impact assessment and human rights, environmental, and social elements, this section first introduces the economic analysis independently, investigating impacts of the four policy options. Thereafter, the study follows with an analysis of each policy option and their specific impacts on social elements, human rights, and environmental concerns.

It is important to underline, however, that this assessment of regulatory options discusses rather broad policy options as this is only a preliminary study. It is not possible to assess the potential impacts in more detail until the concrete elements of each policy option have been defined, for example during any consultations on a regulatory proposal. The following impact assessment is therefore to be read in light of these limitations, and should be taken as a general discussion of potential impacts which could arise and should be taken into account if and when a new regulation is designed.[1363]

Moreover, it is important to stress that the assessment aims to quantify impacts where possible, but that the quantification of costs and benefits in impact assessments is often difficult due to the lack of appropriate data. It is especially difficult to quantify impacts for the non-economic impact areas as the quantification and monetization of social and environmental costs and benefits requires sophisticated methodologies and data to estimate approximations and there are only few impact assessments of similar legislations which contain data that can be used for this analysis.

In a report assessing approaches to quantification in impact assessments, a previous study found that in practice the extent of quantification is lower than what could be assumed from official commitments to using cost-benefit analyses and the available guidance on methodologies.[1364] Moreover, the authors point out that methodological

[1363] For example, according to Tool #8 of the European Commission's Better Regulation Toolbox and Guidance, a full-scale IA is most commonly implemented throughout 12 full months. This may be longer or shorter depending on various factors including the significance of the foreseen policy impacts, data availability, and the stakeholder consultation strategy/process. Given the large scope of the study at hand, and depth of collected data via the stakeholder consultation, the team prioritized the analysis from an approach it understood as both most helpful to inform DG JUST's policy approach, as well as feasible given the limitations of a shorter timeframe. See Better Regulation Tool #8, available at: https://ec.europa.eu/info/sites/info/files/file_import/better-regulation-toolbox-8_en_0.pdf

[1364] Thiessen, J. et al. (2013). *Quantifying the Benefits of Regulatory Proposals: International Practice.* Basel: prognos, 2013. In: Deringer, H. (2014). *Cost-benefit analyses in trade regulation: How to assess the health impacts of non-tariff measures?*

challenges arise particularly for impacts, which are not economic, such as "societal" impacts in the form of social and environmental impacts. Assessing the extent of quantification in impact assessments, the European Commission's Regulatory Scrutiny Board also found in its latest report that approximately 25% of EU impact assessments fully quantify costs and benefits, but at the same time 20% of the reports are purely qualitative.[1365] The remaining reports use partial quantification. Similarly, a recent report of the RSB/SG/JRC Working Group lists quantification tables of selected impact assessments in 2017 and 2016. The list shows that, on the one hand, not many impact assessments provide comprehensive quantitative information on costs and benefits and those which do, provide estimates mainly for economic costs and benefits only.[1366]

In addition, due to the relative newness of relevant laws which require due diligence as a legal standard of care, it has proven challenging to find impact assessments which have been carried out for similar legislation, and where these were found they did not necessarily include information and/or data which could be used for this analysis. Especially when using quantitative estimates from other studies or impact assessments it is important that the underlying activities or elements of the regulation on which such estimates are based are very similar to those in the assessed regulatory options in this impact assessment. Otherwise, if the estimates are based on activities or elements which are too different, such estimates cannot be used as proxies for possible costs or benefits.

Furthermore, not all studies which refer to links between sustainable business activities and company performance in the long and short term are informative for the purposes of considering potential impacts on companies, because these studies are usually about wider "sustainability" questions and their impact on company performance. However, due diligence as a legal standard or duty of care in this case requires companies to exercise the care required to prevent and address external harm, regardless of whether such harm is beneficial, detrimental or neutral to the company's performance in the long or short run. In this way, due diligence in this impact assessment differs, for example, from the requirements of the EU NFRD, which requires information relating to the company's performance.

The following table provides an overview of key regulations and the available impact assessments as well as the information contained therein relating to the assessed impact areas. As Table 8.24 shows, for national laws there are no impact assessments which are publicly available (or which have been carried out). In addition, since this is a very new area of regulation, information on potential impacts is scarce. A recent research paper on human rights and environmental due diligence legislation concludes that most legislations on disclosure and due diligence policies have only been "implemented recently, or are currently underway, meaning impact assessments and evaluations are expected in the coming years in several countries".

MILE Thesis. Bern: WTI Institute. Retrieved from: https://www.wti.org/research/publications/952/cost-benefit-analyses-in-trade-regulation-how-to-assess-the-health-impacts-of-non-tariff-measures/
[1365] European Commission (2019). *Regulatory Scrutiny Board – Annual Report 2018*. Retrieved from: https://ec.europa.eu/info/publications/regulatory-scrutiny-board-annual-report-2018_en.
[1366] European Commission (2018). Report of the RSB/SG/JRC Working Group - Quantification in Commission Impact Assessments and Evaluations. Retrieved from: https://ec.europa.eu/info/publications/report-rsb-sg-jrc-working-group-quantification-commission-impact-assessments-and-evaluations_en.

Table 8.24 Overview of impact assessments of key regulations and covered impact areas

Impact Assessments of Key Legislation	Economic Impacts	Social Impacts	Impacts on Human Rights	Environmental Impacts	Impacts on Public Authorities
EU Commission Impact Assessment on Additional Options to Combat Illegal Logging (2008)	The assessment of economic benefits is based on circumstances (reduction of illegal imports) which are not comparable to the assessed regulatory options. In addition, economic impacts are drawn from a partial equilibrium trade model and the results are therefore very specific to the modelled circumstances and particularities of the forest industry.	The assessed regulatory options and sectoral focus are too different in order to use the results for this impact assessment. Focus is on sectoral employment effects in forest industry based on impacts on production resulting from a partial equilibrium trade model. Social aspects relating to equal opportunities, private life and access to social welfare systems are considered to not be affected and are not discussed.	The IA does not directly assess human rights impacts. However, Option 4B requires a certification of legality for market operations of timber products. The absence of an internationally agreed definition of legality and the issue of what would constitute a credible proof of it would represent a considerable challenge as there would be a risk of accepting "legality" documents from countries with human rights abuses. This might indirectly negatively impact responsibility towards rights holders as those in violation might receive illegitimate credibility.	While to different extents, all policy options are expected to reduce the volume of illegal logging, decreasing destructive practices such as: • high-grading, soil and stand damage; • depletion of the forest resource base and threatening remaining intact sites; • deforestation, erosion sedimentation and variations in hydrological regimes that lead to degradation of land and water resources; • loss of forest cover due to informal roads constructed by illegal loggers; • and recurrent forest fires.	Estimated regulatory cost refers to government activities which are not representative of the potential activities under the assessed regulatory options in this impact assessment.
EU Commission Impact Assessment of EU NFRD Proposal (2013)	General discussion of economic benefits referenced in the analysis, no quantification.	Vey broad and general discussion of various possible social impacts without any details or quantifications. Possible	Mandatory NFR is expected to have a beneficial impact on the following fundamental rights:	The preferred options of reporting requirements are expected to provide the following positive environmental impacts:	No considerable cost expected for EU or MS budgets.

		employment effect discussed generally without any details, quantification or data.	• the workers' right to information (Article 27 of the Charter of Fundamental Rights of the EU137) • human rights awareness within companies • reducing instances of EU company involvement in human rights infringements • the right to non-discrimination (Article 21 of the EU Charter) • Equality between women and men (Article 23). • Freedom to choose an occupation and right to engage in work (Article 15) • Freedom of expression and information (Article 11)	• More transparency; • better quality of information on companies' environmental performance; • increase in environmental awareness; • increase in reputational costs for misbehaviour	
EU Conflict Minerals – Assessment of Due Diligence Compliance Cost, Benefit and Related Effects on Selected Operators in Relation to the Responsible Sourcing of Selected Minerals (2014)	General discussion of economic benefits referenced in the analysis, no quantification.	Impact assessment only describes general survey results, no detailed discussion of social impacts or quantification of costs.	Both voluntary and mandatory importing certifications would provide indirect benefits by increasing demand for ethically sourced minerals. However, mandatory certifications may incentivize companies to seek least burdensome path to compliance which could	Both voluntary and mandatory importing certifications would provide indirect benefits by increasing demand for sustainably sourced minerals. However, mandatory certifications may incentivize companies to seek least burdensome path to compliance which could	Estimated administrative impact for European Commission and Member State authorities used in the analysis.

			divert negative impacts to other companies. An import ban nonetheless without a compliance certificate is expected to have positive impacts through increased government intervention.	divert negative impacts to other companies. An import ban nonetheless without a compliance certificate is expected to have positive impacts through increased government intervention.	
EU Impact Assessment on Proposed EU Regulation on Sustainable Investment (2018)	Economic benefits discussed rather generally not specifically for firm-level. Data provided only for specific aspects such as cost of ESG integration.	Social impacts not assessed in detail. No employment effects discussed, no quantifications.	Options 2 and 3 on harmonization on environmental taxonomy both might potentially have positive effects on human rights as the issue of uncertainty on what sustainable investments are is partially addressed and would help end-investors identify sustainable activities. Option 3b on Mandatory disclosures on sustainability objectives is expected to increase transparency on achievement of such objectives.	Options 2 and 3 on harmonization on environmental taxonomy both might potentially have positive environmental effects as the issue of uncertainty on what sustainable investments are is partially addressed and would help end-investors identify sustainable activities. Option 3b on Mandatory disclosures on sustainability objectives is expected to increase transparency on achievement of such objectives.	No impacts on public authorities assessed, only process of evaluation described but no cost estimates provided.
EU Commission Action Plan on Financing Sustainable Growth – PRI Assessment of the Reform Areas for PRI Signatories	Only an action plan, no impact assessment. No information on economic impacts.	Only an action plan, no impact assessment. No information on social impacts.	Only an action plan, no impact assessment. No information on human rights impacts.	Only an action plan, no impact assessment. No information on environmental impacts.	Only an action plan, no impact assessment. No information on impacts on public authorities.
EU Impact Assessment of Directive 2008/99/EC on	Impacts described very generally and no	Impact on employment or other social impacts	No discussion on direct human rights impacts.	Both options 2 (encourage cooperation)	Impacts described very generally and no

the protection of the environment through criminal law (evaluation ongoing[1367])	quantification is provided.	not discussed.	However, possible indirect impacts include increase in human health as harmonization of environmental offence definitions may facilitate the targeting of most serious cases.	and 3 (set regulatory standards) can be expected to have positive impacts. Both would increase public awareness and increased sanction levels and scopes of liability for environmental protection.	quantification of costs is provided.
EFFACE Synthesis Report (2016) on the ECD	Does not assess economic impacts or benefits for firms.	No discussion of social or employment impacts.	No discussion of human rights impacts.		Briefly compares expected costs for the state from different sanction systems but does not provide any cost estimates.
EU Impact Assessment of Directive 2012/18/EU - Seveso III Directive	Economic benefits for operators described only very generally.	Impact on employment or other social impacts not discussed except for few sentences.	Impacts on human rights under all possible options of the Seveso Directive depend on how many establishments will fall under the Directive. Specifically, under policy option 4 which establishes information access to the public, there would be positive impacts on protection levels for human health.	Effects on environmental impacts not discussed in detail.	Limited usefulness of described activities of public authorities, costs related to provision of information to the public and information management system partly used.
Report on Implementation of EU Directive 2004/35/EC -	Economic benefits to	Does not assess any social or employment	The ELD increases recognition of rights	Because the ELD is not coordinated or	Report concludes that not possible to draw sound

[1367] See: https://ec.europa.eu/info/law/better-regulation/initiatives/ares-2018-4981980_en

Environmental Liability Directive (no IA available)	firms are not discussed.	impacts.	holders under Articles 7(4) and 12 which confirm a person who could be affected by the damage, or with a legitimate interest, as well as environmental NGOs, have rights to request and receive information regarding the implementation of prevention and remedial measures.	harmonised with the Habitats Directive, any positive impacts for environmental protection are at risk. While a key added value of the ELD is the possibility to attribute strict liability to an operator for damage to biodiversity, the distinction between strict liability and fault based liability across different types of activities makes it difficult to prove causal links.	conclusions on administrative costs.
EU Timber Regulation Implementation Report (2017)	No discussion on economic benefits.	No discussion on social and employment impacts	No discussion on human rights impacts.	The EUTR demonstrated to be highly relevant for tackling illegal logging and related trade by changing market behaviour patterns and freeing supply chains from illegally harvested timber. Notably, the EUTR establishes uniform rules, and is coherent with other relevant policy instruments.	MS reported on human and financial resources of Competent Authorities but data quality very low.
French Vigilance Law	No available IA	No available IA	No available IA	No available IA	No available IA
Dutch Child Labour DD Law	No available IA	No available IA	No available IA	No available IA	No available IA

Italian Decree on Due Diligence	No available IA	No available IA	No available IA	No available IA	No available IA
Spanish Law on Environment + HR	No available IA The economic report of the 2008 Draft of reform of the Criminal Code was not presented.[1368]	No available IA	No available IA	No available IA	No available IA
Swiss Advanced Legislative Proposal	No available IA	No available IA	No available IA	No available IA	No available IA

[1368] In a congress report on the Draft it says: "A second element that leads this Parliamentary Group to present this amendment to the whole is the absence of an economic report…" Source: *http://www.congreso.es/public_oficial/L9/CONG/BOCG/A/A_052-09* .PDF, p. 7. . Something similar is indicated in a report by the Judiciary.

3.1 Economic Impacts across Regulatory Options

3.1.1 General remarks

We considered several impact assessments of related EU regulations to inform the methodology of this economic impact assessment. However, we note that the suitability of impact assessments of existing studies, e.g. the EU Conflict Minerals Regulation, the EU Non-financial Reporting Directive, the EU Timber Regulation, the Directive on the Protection of the Environment through Criminal Law and the Directive on the Control of Major-accident Hazards Involving Dangerous Substances, is limited. Generally, while some of these assessments provide quantitative estimates, others discuss impacts only qualitatively.

- Detailed descriptions of the impact assessments conducted for the EU Conflict Minerals Regulation and the EU Non-financial Reporting Directive are provided in the literature review. The impact assessments of these regulations have some commonalities, but also show differences regarding the methodologies applied by the consultants. Both studies' shortages generally include a lack of publicly available industry data and a high variation in the quantitative and qualitative information collected through surveys and consultations. Costs were usually expressed in annual numbers on a per company basis. The authors also differentiated between large companies and SMEs (typically companies with less and more than 250 employees, according to Eurostat definitions).[1369] Cost estimates are based on survey data or publicly available information. Estimates were provided for internal labour cost (staff cost or staff time) and external costs (e.g. cost for consultants, external auditing costs, training costs).

- The impact assessment of the EU Timber Regulation provides cost estimates for the EU level (EU aggregate). Considering different technological tracking solutions, several cost estimates were calculated on a per cubic metre basis for traded wood products. Firm-level economic benefits of the EU Timber Regulation were assessed qualitatively.

- For the Directive on the Control of Major-accident Hazards Involving Dangerous Substances, ranges of 'administrative cost' estimates have been taken from a number of separate studies, while the economic benefits have been discussed qualitatively. The estimates are rather rudimentary and, as noted by the authors of the study, should be interpreted with caution.

- For the Directive on the Protection of the Environment through Criminal Law, both firm-level cost and benefits have been discussed qualitatively. The impact assessment does not provide quantitative estimates.

The economic analysis is to a large extent based on the responses of business stakeholders, which come with a number of shortages:

[1369] In the impact assessment of the EU Non-financial Reporting Directive, all options analysed are intended to cover only companies having more than 500 employees. Consequently, no administrative burden was found for SMEs.

1) Due to the lack of existing examples of DD regulation, and the preliminary nature of this study which does aim to formulate a regulatory proposal, the regulatory or policy options are only expressed in broad terms. Many stakeholders have different experiences with laws that relate to due diligence reporting and administrative requirements. In addition, stakeholders do not yet have the benefit of court judgments which clarify how recent laws such as the French Duty of Vigilance Law will be applied, and how their companies should respond. This results in varying expectations among the respondents with regard to the legal obligations and companies' activities necessary to comply with these obligations. The time and cost estimates given by the respondents may therefore not reflect the real additional burden that would result from DD activities. It should be noted that respondents may have over- and underestimated the impact of the outlined policy options, not least due to the fact that there is relatively little or no existing examples of DD regulation which informs their experiences and knowledge. This may explain why the data provided by large companies (1000+) which are already undertaking DD appears to be most reliable, as these are the companies which are most likely to be subject to existing regulation (which applies predominantly to large companies), as well as existing industry standards.

2) It is also noted that the survey indicated that the majority of respondents which are responsible for due diligence are within the corporate social responsibility teams of their companies. These respondents would not necessarily be able to give more adequate time and/or cost estimates relating to new legal implications. Cost and person-day requirements critically depend on many individual company characteristics, such as company size, the number of suppliers, (B2B) customers or the degree of software utilisation for corporate management in general and value chain management in particular.

3) Company-level impact analysis would take a considerable amount of time for corporate planners and controllers, particularly in larger companies. It is questionable whether such analyses indeed informed respondents' estimations, given the short periods of reply.

4) The data given by the respondents is patchy. As outlined above, the data also show a high level of variation within and among companies of different size classes. At the same time, the correlations with proxies for company size (e.g. the number of sectors) and the size of the value chain (e.g. the number of suppliers) are low. In addition, data on company-specific supply chains is not publicly available. It is therefore difficult to control and differentiate for supply chain size effects.

5) Due to the lack of more adequate data, and similar to other studies, we classify companies' size according to the number of employees. At the same time, it should be noted that the extent of a company's value chains does not necessarily correlate with the number of its employees or the number of its suppliers and/or customers. Some services companies might be human capital-intensive (employees-intensive), but source material from a low number of suppliers. By contrast, manufacturers that rely to a substantial degree on automation might have a low number of their own employees, but source materials from a great number of suppliers.

6) The numerical estimates given by the respondents do not reflect where respondents' companies source their products and services. In other words, we cannot account for companies that are to a large extend engaged in developing countries' markets, where some of the most prominent human rights and environmental risks may occur. It is assumed that companies sourcing in developing countries are likely to face higher compliance costs than companies that exclusively source from and sell on local markets within the EU. For the former group of companies, our estimates might underestimate the time and cost burden resulting from DD activities. Whilst recognising these limitations, it should also be noted that companies' most prominent human rights and environmental risks do not take place exclusively outside of the EU. For example, exploitation of migrant workers and modern slavery within the EU are increasingly well-documented. As a result of the complexity and non-transparency of globalised supply chains, there is a general lack of knowledge about the real impacts of companies' supply chains, whether inside or outside of the EU. This is another limitation of the data relied on in this study.

7) Moreover, it is important to keep in mind that the same legal duty could manifest differently in practice for different economic operators (e.g. producers, manufacturers, authorised representatives, importers and distributors). Although the legal duty would be the same independently from where the company is in the value chain, the economic and activity burden could differ depending on the risk and context of a company. As a result, in practice the duty could have different economic impacts depending on the company's place in the chain, the due diligence already undertaken by others, its assessment and prioritisation of its risks, and other risk factors.

8) It should be noted that other studies also suffer from these limitations. It should also be noted that we developed estimates that go beyond most existing studies. For firm-level costs, for example, we provide estimates for large companies, SMEs as well as aggregate numbers for some sectors and the corresponding EU aggregates.

It should also be noted that these economic impacts are measured in relation to a change from the status quo. However, the status quo is expected to change as the various fast-moving developments noted elsewhere in this study continue. These include legal developments around possible mandatory due diligence law in Member States, and increasing investor and financial focus on due diligence requirements. Within this context, it is critical to remember that stakeholders across the spectrum have expressed a discontent with the current legal landscape. Survey results show that stakeholders perceive the current laws in this area as not being effective, efficient and clear, and have noted various disadvantages (including economic impacts) that companies suffer from as a result. In this context, the Market Practices findings show that companies expect certain benefits to arise from a mandatory duty which applies on a general basis, including a level playing field and increased leverage through a non-negotiable standard. While it is not possible to quantify these benefits at such an early stage, it should be emphasised that these benefits may be significant, insofar as they could improve the costs relating to risks that are present in the current status quo.

3.1.2 Company-level Costs

The company-level cost impact analysis is mainly based on responses received from 336 businesses. In the survey, companies were required to indicate the number of person-days and costs related to certain human rights and environmental due diligence (DD) activities. The respondents were not asked to provide estimates about the impact of economic inefficiencies resulting from changes in companies' supply chain management due to DD activities.

The respondents were asked to provide numbers for four policy scenarios:

- Option 1: No policy change
- Option 2: Voluntary guidelines
- Option 3: Mandatory DD reporting
- Option 4: Mandatory DD throughout value chains

For person-days, the following due diligence and reporting activities were taken into consideration:

1) Impact assessments & tracking effectiveness of actions
2) Training
3) Incorporation of standards into contracts / codes of conduct
4) Audits / investigations
5) Leverage (suppliers / investee companies / third parties) & collective engagement
6) Reporting activities

Respondents were also asked to indicate the total number of person-days estimated for DD activities ("Alternative: Total days" in the business stakeholder survey).

For costs per activity, the following cost types were taken into consideration:

1) Cost of labour
2) Overheads
3) Cost of outsourcing / external services (including auditors & experts)
4) Cost of reporting
5) Other costs

Respondents were also asked to indicate the total cost estimates ("Alternative: Total cost" in the business stakeholder survey).

Table 8.25 provides summary statistics for the number of respondents by size class and type of DD already undertaken. While 159 respondents did not indicate whether their companies already conduct certain DD activities, 137 respondents indicated that their companies already undertake some DD activities. 13 respondents stated that their companies do not yet undertake any form of DD activity for human rights or environmental impacts. 25 respondents indicated that they "do not know" whether their companies conduct any such DD activities.

Generally, the highest number of due diligence activities already undertaken is reported by large companies with 1,000 and more employees (171 respondents). 63% of these companies report that they already conduct some DD activities. 30% of these companies report to already undertake "Human rights due diligence which takes into account all human rights (including environment)". 27% report to already undertake "Human rights due diligence, but only in certain areas (for example health & safety, labour, non-discrimination & equality, environmental, land rights & indigenous communities), and 4% state to conduct "Environmental / climate change due diligence (not extending to other human rights)".

At the same time, smaller companies with more than 50 but less than 1,000 employees (61 respondents) report to conduct certain DD activities. 18% of these companies report that they already conduct "Human rights due diligence which takes into account all human rights (including environment)" and 15% report to already undertake "Human rights due diligence, but only in certain areas (for example health & safety, labour, non-discrimination & equality, environmental, land rights & indigenous communities). Smaller companies (28 respondents) with less than 50 employees do generally not conduct any due diligence activities.

Table 8.25: Respondents by size class and type of DD already undertaken

Company size	Total	Human rights due diligence which takes into account all human rights (including environment)	Human rights due diligence, but only in certain areas (for example health and safety, labour, non-discrimination and equality, environmental, land rights and indigenous communities)	Environmental / climate change due diligence (not extending to other human rights)	My company does not / has not yet undertaken any form of due diligence for any human rights or environmental impacts	Do not know
1000+ employees	171	51	47	6	3	13
500-1000 employees	19	5	1	2	1	2
250-500 employees	17	0	3	2	4	2
50-249 employees	25	6	5	3	3	1
10-49 employees	8	1	2	0	0	1
0-9 employees	20	1	1	0	2	6
No indication	74	1	0	0	0	0
Total	**334**	**65**	**59**	**13**	**13**	**25**

Source: Business and Stakeholder Surveys. Note the 159 companies did not reply to the question about due diligence activities already undertaken by their company.

The next sections provide graphical illustrations for the development of the number and allocation of person-days by policy option. Accounting for outliers in the data, we outline the empirical median values for the full sample of companies as well as the full sample of large companies and large companies that, according to their stated information, already undertake full DD activities.[1370] Mean values as well as lower and upper quartiles are reported in the literature review of the first interim report. For the sake of completeness, we also report numbers for smaller companies. Due to the low number of responses for small company respondents, numbers for smaller companies should be interpreted with caution.

The given estimates for the number of person-days turn out to be patchy. Many companies only provided estimates for some DD activities. Others only provided estimates for total person-days. For some activities we detected large differences between mean and median values in both the indicated person-day and total cost estimates. Generally, the highest number of person-day estimates is available for large companies (500-1,000 and 1000+ employees). By contrast, only little data is available for companies that do not yet conduct such DD, mainly medium-sized and small companies with 0 to 500 employees.

About 30% of companies with more than 1,000 employees already undertake "Human rights due diligence which takes into account all human rights (including environment) and some 27% of these companies already undertake "Human rights due diligence, but only in certain areas (for example health & safety, labour, non-discrimination & equality, environmental, land rights & indigenous communities)". The most consistent data was provided by respondents from companies that already conduct full human rights and environmental DD or certain parts of it.

- **Estimated person days by activity and policy option**

<u>Estimated person days in the full sample of companies</u>

As shown by Figure 8.1 for the full sample of respondents (which is comprised of experienced and less experienced respondents with respect to DD activities), "Impact assessments & tracking effectiveness of actions" (e.g., 10 person-days per month for mandatory DD) and "Audits / investigations" (e.g., 10 person-days for mandatory DD) are the most person-day-intensive activities. This is followed by "Training" activities e.g., 10 person-days for mandatory DD) and activities related to "Leverage (suppliers / investee companies / third parties) and collective engagement" (e.g., 6.5 person-days for mandatory DD). Mere reporting activities are less person-day intensive.

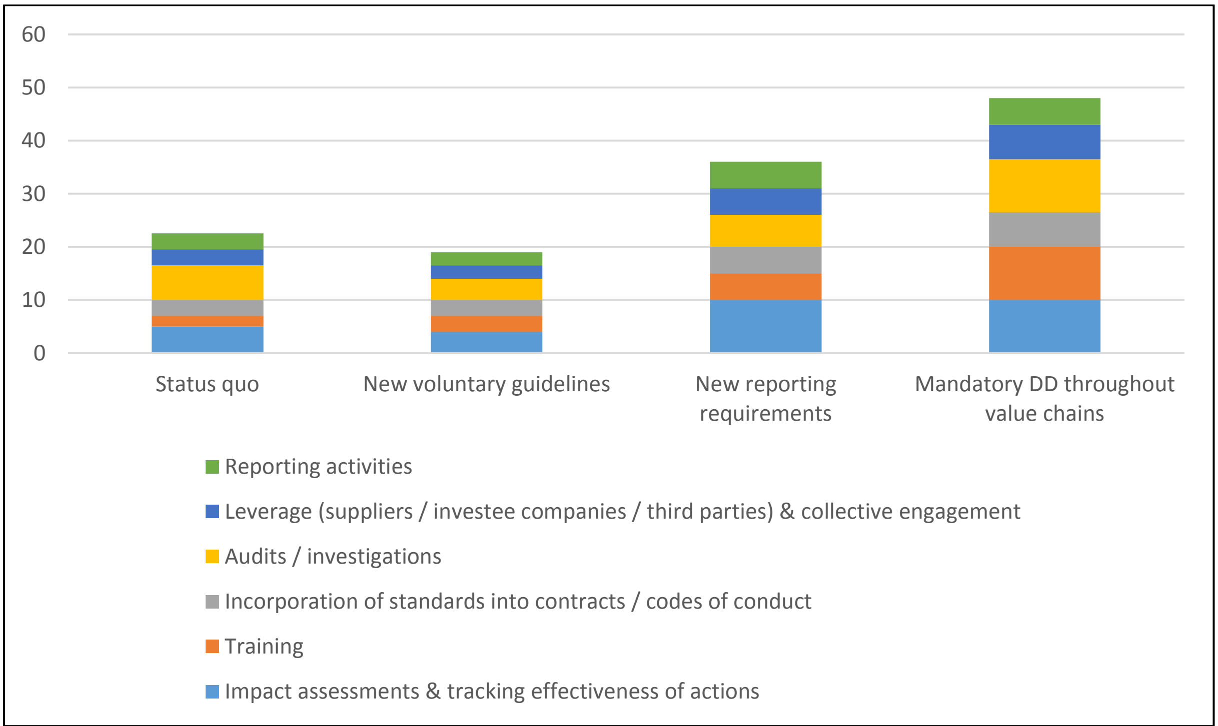
The numbers also indicate that many companies already conduct DD activities that go beyond complying with voluntary guidelines. The aggregate number of person-days indicated for compliance with new voluntary guidelines under regulatory Option 2 is somewhat lower than what companies state for the status quo activities under Option 1 (i.e. the sum of person-days stated for individual activities). However, the total cost estimates ("Alternative: Total days" in the survey) indicate that the number of required person-days is higher for activities under "New voluntary guidelines" when compared to the "Status quo". The slight decrease in the number of required person-days for "New

[1370] Accounting for outliers in the data, we outline the empirical median values for the full sample of companies as well as the full sample of large companies and large companies that, according to their stated information, already undertake full DD activities (the empirical mean values, which are often distorted by outliers, are reported in the first interim report).

voluntary guidelines” results from differences in the respondents: some respondents who proved estimates for the “Status quo” did not provide estimates for “New voluntary guidelines” and vice versa. For those companies that indicated person-day requirements on a DD activity basis, the numbers indicate that companies already conduct activities that likely go beyond those prescribed by voluntary guidelines. For those companies that indicated total person-day requirements, the numbers reflect less experienced companies’ expectations regarding the labour cost impact resulting from voluntary guidelines, which is, as expected, estimated to be higher than for the status quo situation. At the same time, the increase in the number of person-days required for mandatory DD reporting and mandatory DD throughout companies’ value chains is also in line with our expectations: more comprehensive DD activities would require additional person-days compared to the status quo.

Compared to the status quo, the increase in estimated person-day requirements is about 100% if companies would have to undertake mandatory DD throughout their value chains in terms of regulatory Option 4. Compared to the status quo, the increase in person-days required is about 50% if companies would have to comply with new reporting requirements only in terms of regulatory Option 3. It should be noted a policy shift from reporting requirements to mandatory DD throughout companies’ value chains would result in relatively high increases in the person-days required particularly for trainings and audits/investigations.

Figure 8.1: Development of number and allocation of person-days by policy option, all business respondents (in person-days per month)



Source: Business and Stakeholder Surveys. Numbers indicated: median values for person-days (8 working hours/day) per month.

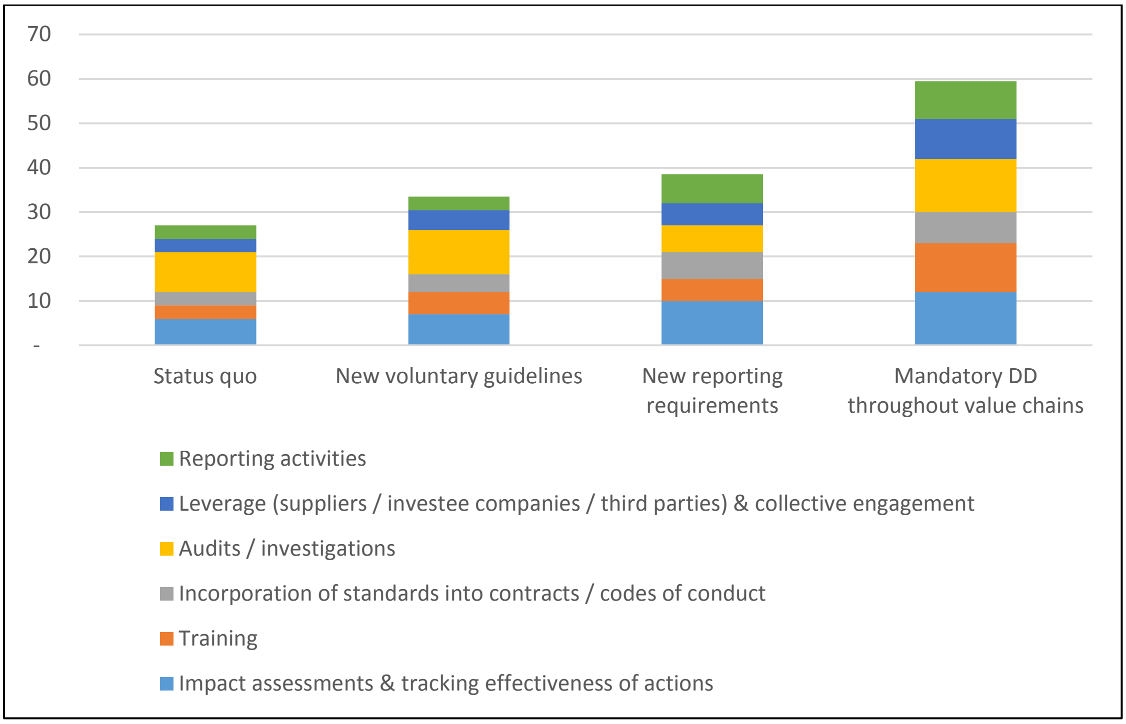
Estimated person-days in the full sample of all large companies (1000+ employees)

As shown by Figure 8.2, the person-day requirements of large companies are generally higher than the average and median values of the full sample of companies. This is because large companies tend to have more DD requirements because of their relative size, e.g. the number of business divisions and the number of suppliers and customers. At the same time, this sample of companies included companies that are already undertaking DD and are therefore likely to have more realistic understanding of the costs involved.

At the same time, similar patterns apply for the relative allocation of estimated person-days. The responses from large companies with 1,000 or more employees indicate that "Impact assessments & tracking effectiveness of actions" (e.g., 12 person-days for mandatory DD per month) and "Audits / investigations" (e.g., 12 person-days for mandatory DD) are the most person-day-intensive activities. "Training" activities and activities related to "Leverage (suppliers / investee companies / third parties) & collective engagement" (e.g., 9 person-days for mandatory DD) become absolutely and relatively more person-day-intensive for new reporting requirements and mandatory DD throughout companies' value chains. The aggregate number of person-days indicated for compliance with new voluntary guidelines is somewhat higher than what companies state for the status quo (i.e. the sum of person-days stated for individual) activities. The same pattern applies for total cost estimates ("Alternative: Total days" in the survey), which also indicate that the number of required person-days is higher for activities under new voluntary guidelines compared to the status quo.

At the same time, the number of person-days required for new reporting requirements and mandatory DD throughout companies' value chains would require significantly more person-days compared to the status quo. Compared to the status quo, the number of person-days more than doubles (from 27 to 60 person-days per month) if companies would have to undertake mandatory DD throughout their value chains (Option 4). Compared to the status quo, the increase in person-days required is about 40% if companies would only have to comply with new DD reporting requirements (Option 3) (from 27 to 39 person-days). It should be noted a policy shift from new reporting requirements to mandatory DD throughout companies' value chains would result in relatively high increases in the person-days required for "Trainings" (from 3 to 11 person-days) and "Audits / investigations" (from 6 to 12 person-days).

Figure 8.2: Development of number and allocation of person-days by policy option, total of companies with 1000+ employees (in person-days per month)



Source: Business and Stakeholder Surveys. Numbers indicated: median values for person-days (8 working hours/day) per month.

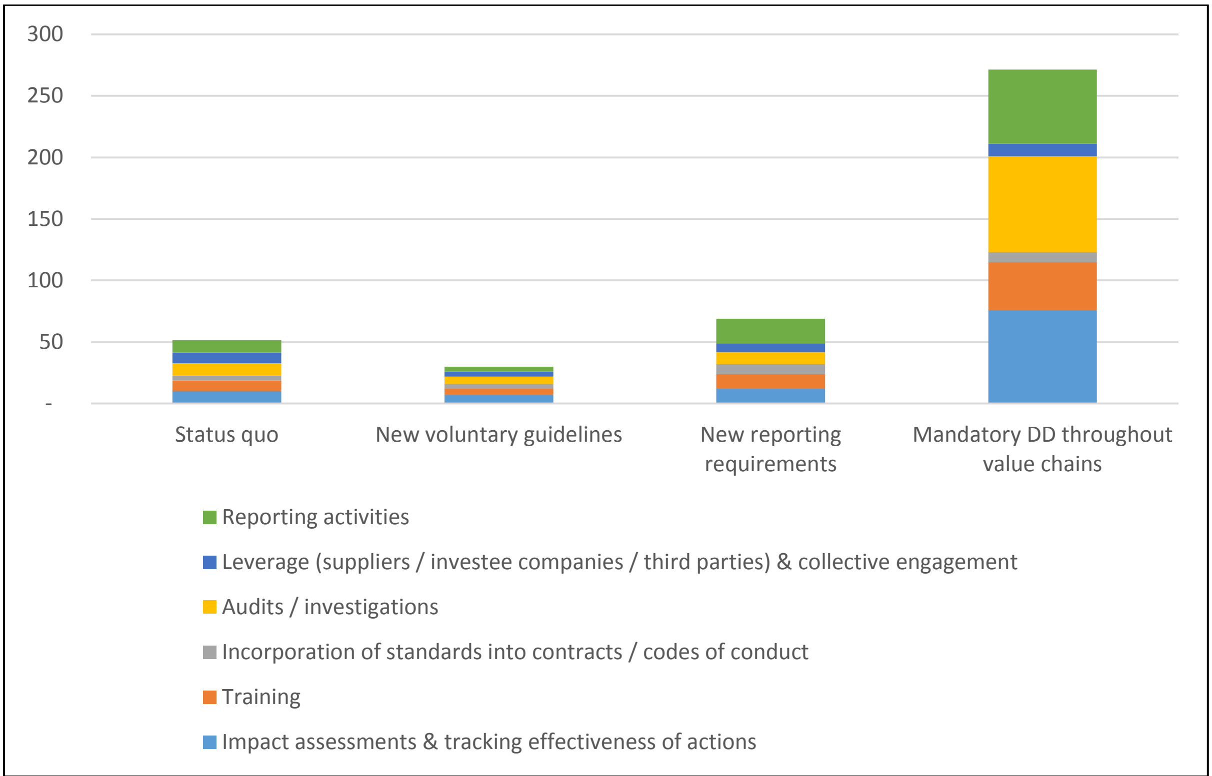
<u>Estimated person-days in the full sample of large companies (1,000+ employees) that already conduct "Human rights due diligence which takes into account all human rights (including environment)"</u>

As shown by Figure 8.3, relatively high numbers for required person-days are reported by large companies that already undertake certain "Human rights due diligence which takes into account all human rights (including environment)". Among these companies, "Audits / investigations" are most person-day-intensive (e.g., 78 person-days for mandatory DD) under the status quo, followed by "Impact assessments & tracking effectiveness of actions" (e.g., 76 person-days for mandatory DD) and "Reporting activities" (e.g., 60 person-days for mandatory DD). At the same time, these companies report only a slight increase in person-days required for new mandatory reporting requirements, but a rather substantial increase in person-days required for mandatory DD throughout companies' value chains. Compared to the status-quo, the total of person-days required for individual activities quintuples (from 52 to 271 person-days) for mandatory DD throughout companies' value chains. The slight decrease in the number of required person-days for "New voluntary guidelines" results from differences in the respondents: some respondents who proved estimates for the "Status quo" did not provide estimates for "New voluntary guidelines" and vice versa.

The stated number of person-days required for "Impact assessments & tracking effectiveness of actions" (from 10 to 76 person-days), "Audits / investigations" (from 10 to 78 person-days), "reporting activities" (from 10 to 60 person-days) and "Training" (from 9 to 39 person-days) activities increases tremendously for mandatory DD throughout companies' value chains. By contrast, relatively low increases are reported for activities related to the "Incorporation of standards into contracts / codes of conduct" as well as "Leveraging (suppliers / investee companies / third parties) & collective engagement".

It should be noted that of all the respondents groups, the estimates provided by this group of large companies, i.e. large companies that already undertake due diligence, appear to be most consistent with respect to the rise in person-day requirements according to the escalation of the policy obligations, the (broad) scope of the regulations and the activities companies would have to undertake to ensure regulatory compliance. In particular, the patterns in the data provided by those which are already undertaking DD activities are different to those indicated by the full sample, which also includes companies with little experience in DD activities. Since these estimates were given by large companies (with more than 1,000 employees) that can already draw on their own experiences of DD and their empirical data, we consider the data provided by large (1000+ employees) companies that are already undertaking DD most relevant for the ongoing analysis. At the same time, we note that the size of these companies in terms of revenues is very high. The median revenue of the respondents that provided both annual revenue data and person-day estimates for the available policy options is 11.5 billion EUR. The average revenue of the respondents that provided both annual revenue data and person-day estimates for the available policy options is 29.3 billion EUR.

Figure 8.3: Development of number and allocation of person-days by policy option, companies with 1,000+ employees that already conduct "Human rights due diligence which takes into account all human rights (including environment)" (in person-days per month)



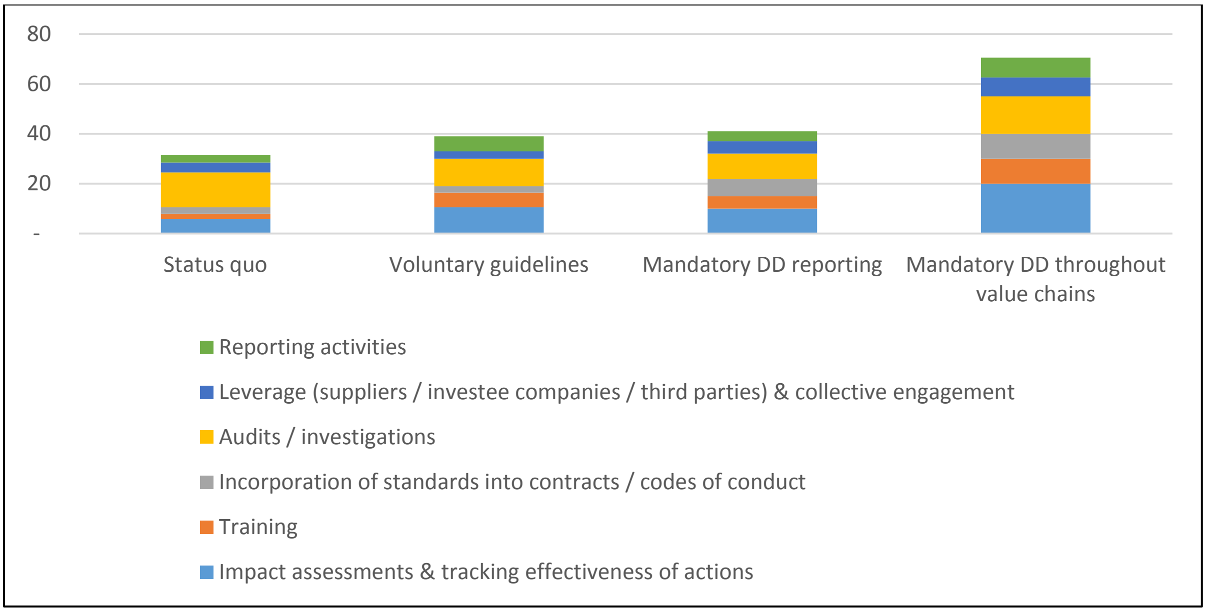
Source: Business and Stakeholder Survey. Numbers indicated: median values for person-days (8 working hours/day) per month. Note that the median revenue of the respondents that provided both annual revenue data and person-day estimates for the available policy options is 11.5 billion

EUR. The average revenue of the respondents that provided both annual revenue data and person-day estimates for the available policy options is 29.3 billion EUR.

Estimated person-days in the sample of companies with 50 to 1,000 employees that already conduct "Human rights due diligence which takes into account all human rights (including environment)"

The estimates for companies with 50 to 1,000 employees that already conduct "Human rights due diligence which takes into account all human rights (including environment)" indicate that "Impact assessments & tracking effectiveness of actions" (e.g., 20 person-days for mandatory DD) and "Audits / investigations" (e.g., 15 person-days for mandatory DD) are the most person-day-intensive activities (see Figure 8.4). Compared to the status quo, the number of required person-days would more than double as the result of a policy shift towards mandatory DD throughout companies' value chain. At the same time, we note that the size of the respondents' companies in terms of revenues is substantially lower than those of large company respondents (1,000+ employees). The median revenue of the respondents that provided both annual revenue data and person-day estimates for the available policy options is 128 million EUR. The average revenue of the respondents that provided both annual revenue data and person-day estimates for the available policy options is 154 million EUR.

Figure 8.4: Development of number and allocation of person-days by policy option, companies with 50-1,000 employees that already conduct "Human rights due diligence which takes into account all human rights (including environment)"

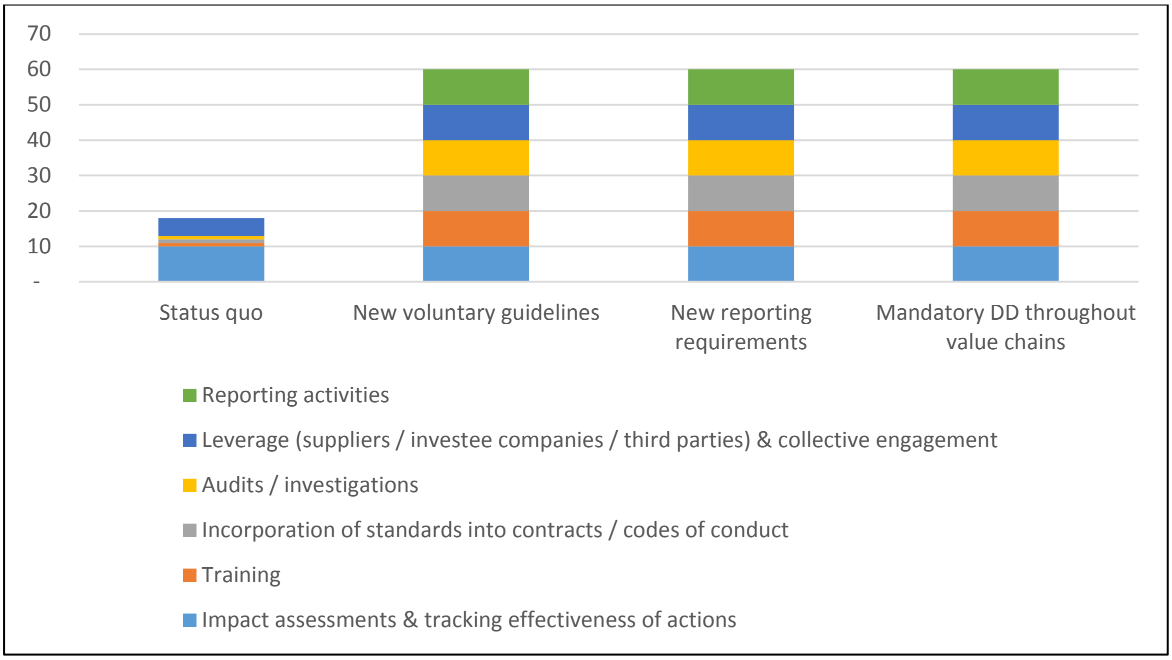


Source: Business and Stakeholder Surveys. Numbers indicated: median values for person-days (8 working hours/day) per month.

Estimated person-days in the sample of companies with less than 50 employees

Due to the lack of data, the person-day estimates provided by small companies with less than 50 employees should be also interpreted with caution. Only one company with less than 50 employees provided estimates for person-days by activity under the status quo. As outlined by Figure 8.5, this company expects an equal distribution of person-days required for DD activities, amounting to 10 person-days for each activity for new voluntary guidelines, new reporting requirements as well as mandatory DD throughout companies' value chain.

Figure 8.5: Development of number and allocation of person-days by policy option, companies with 0-49 employees (in person-days per month)



Source: Business and Stakeholder Surveys. Numbers indicated: median values for person-days (8 working hours/day) per month. Note: These number should be treated with caution. The data reflect the responses of 28 companies of which only two companies provide estimates for the number of person-days required for certain DD activities.

The survey respondents also indicated expected total person-day requirements for the available policy option**.** It should be noted that estimates for total person-day requirement were often given by respondents that did not indicate person-days on a DD activity basis. Table 8.26 provides a comparison of indicated total person-day estimates per month by policy option and company size. For respondents that indicated person-day requirements on a DD activity basis, the numbers provided for total person-days often deviate from the sum of person-days indicated for individual DD activities. At the same time, the numbers generally reflect the same patterns that prevail for individual DD activities, i.e. a rise in required person-days resulting from a rise in DD obligations.

The numbers are generally highest for the total of companies with 1000+ employees that already conduct "Human rights due diligence which takes into account all human rights (including environment)". It should be noted that for all companies with 1,000+ employees that already conduct "Human rights due diligence which takes into account all human rights (including environment)" (13 respondents) the median value, as indicated by Table 8.26 Table 0.1 below, *decreases* for mandatory DD throughout value chains compared to new voluntary reporting requirements. If this pattern was valid, there would be less person-days required for the mandatory DD than for new reporting requirements. We consider these numbers counterintuitive and checked for average values, which indeed point to substantially higher person-day requirements for mandatory DD activities: The mean (average value) increases by about 30% from 293 person-days to 376 person-days for mandatory DD. Accordingly, the responses for this group (13 responses) should be treated with caution. One explanation for this somewhat paradoxical finding is that companies of different sizes indicated different cost estimates, which show a high degree of variation. Due to data gaps, however, we cannot effectively control for size effects.

Table 8.26: Total number of person-days per month, by activity, median values

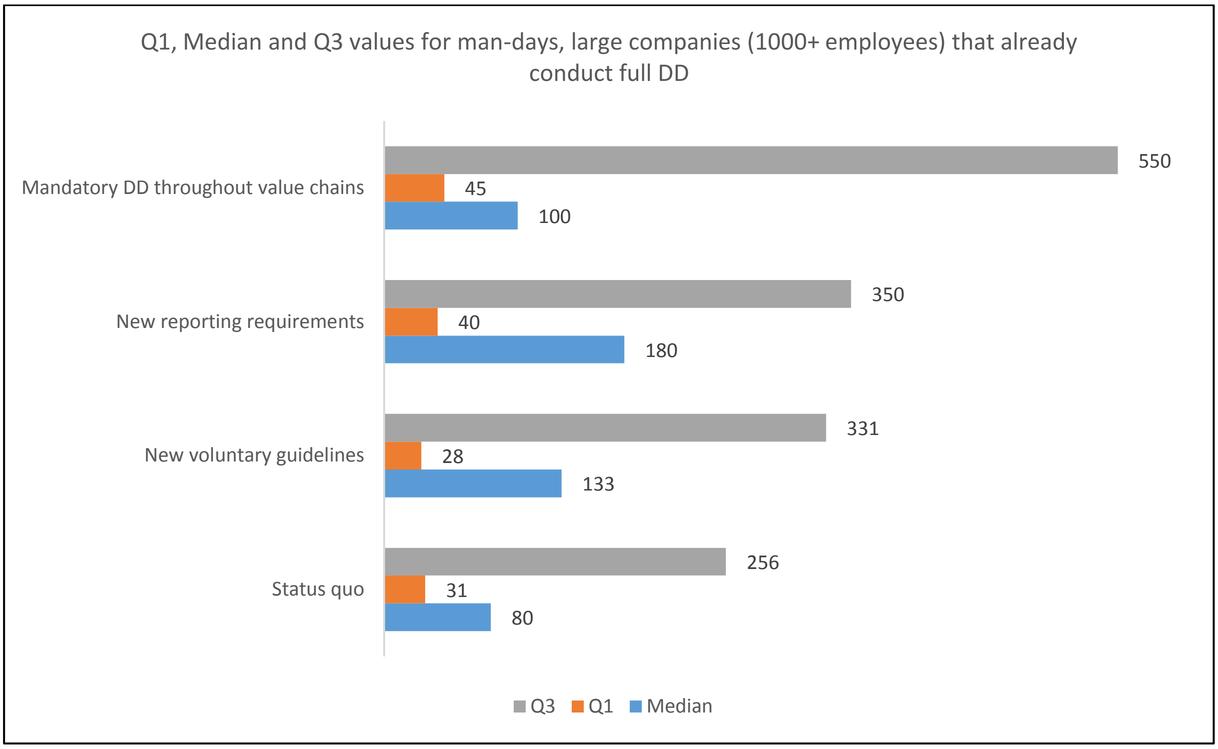
Responses	All business respondents	Total of companies with 1,000+ employees	Total of companies with 1,000+ employees that already conduct "Human rights DD which takes into account all human rights (including environment)"	Companies with 50-1,000 employees that already conduct "Human rights DD which takes into account all human rights (including environment)"	Companies with less than 50 employees
Status quo	22 person-days (46 respondents)	44 person-days (37 respondents)	80 person-days (14 respondents)	24 person-days (1 respondent)	2 person-days (4 respondents)
Voluntary guidelines	33 person-days (39 respondents)	48 person-days (32 respondents)	133 person-days (14 respondents)	-	10 person-days (2 respondents)
Mandatory DD reporting	40 person-days (37 respondents)	56 person-days (30 respondents)	180 person-days (13 respondents)	34 person-days (1 respondent)	10 person-days (4 respondents)
Mandatory DD throughout value chains	56 person-days (33 respondents)	66 person-days (29 respondents)	100 person-days (13 respondents)	-	10 person-days (4 respondents)
Growth rates compared to status quo					
Status quo					
Voluntary guidelines	50%	9%	66%	-	400%
Mandatory DD reporting	82%	26%	125%	42%	400%

Mandatory DD throughout value chains	155%	50%	25%	-	400%

Source: Business and Stakeholder Surveys. Numbers indicated: median values of estimated person-days, based on replies to option “Alternative: Total days”.

Figure 8.6 provides a comparison of the 1st-quartile, median and 3rd-quartile values for indicated total person-day estimates by policy option for large companies (1000+ employees) that already conduct "Human rights due diligence which takes into account all human rights (including environment)". The statistics generally reflect the same patterns that prevail for individual DD activities, i.e. a rise in required person-days resulting from a rise in DD obligations. It should be noted that these companies, which have the most profound experience with DD activities, nevertheless show a relatively high level of variation in the number of person-days required for DD activities. For mandatory DD throughout companies' value chains, the bottom 25% of these companies (Q1 values) report less than 45 person-days, while to top 25% (Q3) report more than 550 person-days. Similar levels of variation are found for the other policy options.

Figure 8.6: Total estimated person-days, large companies (1000+ employees) that already conduct "Human rights due diligence which takes into account all human rights (including environment)"



Source: Business and Stakeholder Survey. Numbers indicated: median, 1st quartile (Q1), 3rd quartile (Q3) values of estimated person-days, based on replies to option "Alternative: Total days".

As shown by Table 0.1 and Table 0.2 in Part IV: Annexures, proxies for company size, i.e. the number of sectors in which companies operate and the number of first tier suppliers, indicate that an increase in business models (number of sectors) or an increase in the number of suppliers (first tier suppliers) *do not necessarily increase or decrease* the number of total person-days needed by large companies for DD activities. According to respondents' estimates there is no significant positive correlation between the number of sectors and the number of required person-days and no significant positive correlation between the number of first tier suppliers and required person-days.

- **Estimated costs by activity and policy option**

As outlined at the beginning of this Section, survey respondents were also asked to provide estimates for the total annual costs by activity. It should be noted that the number of given responses is generally higher for person-day estimates than for cost estimates. This pattern applies for all size classes of companies. For companies with little or no experience in DD activities, the numbers provided for cost estimates are often inconsistent with respect to the escalation of policy obligations under the four policy options. Many companies, especially those with little or no experience in DD activities, stated higher costs for new reporting requirements than for mandatory DD in companies' value chains. The lack of knowledge about the implications of mandatory DD regulation could be explained by the lack of currently existing examples of such regulation, particularly with application to SMEs. In contrast, reporting requirements may already apply to larger companies, which informs their knowledge about the cost implications.

Due to the lack of responses and the inconsistencies in the cost estimates provided by the respondents, we (similar to other impact assessments) consider person-day estimates more representative than estimates for cost figures. Accordingly, the following estimations are based on the person-day estimates given by the respondents.

- **Estimated costs of outsourcing / external services**

While we consider the estimated sum of person-days indicated for individual DD activities a more reliable basis for our estimations, we note that the "Cost of outsourcing / external services (including auditors & experts)" account for a relative high share of the total costs stated by the survey respondents. The reported "Cost of outsourcing / external services (including auditors & experts)" are often the second highest cost component stated by the respondents, whereby other costs stated by the respondents to a large extent overlap with respondents' estimated labour costs, i.e. "Overheads" and the "Costs of reporting". "Other costs", as stated by the survey respondents (<3%).

For the share of "Cost of outsourcing / external services (including auditors & experts)" in the "Cost of labour", Table 8.27 outlines numbers for different groups of business respondents and policy options.

Table 8.27: Share of estimated "Cost of outsourcing / external services (including auditors & experts)" in the estimated "Cost of labour"

	Status quo	New voluntary guidelines	New reporting requirements	Mandatory DD throughout value chains
All business respondents:	9%	34%	17%	25%
Full sample of large companies (1000+ employees)	8%	5%	17%	26%
Companies with 1000+ employees that already conduct "Human rights due diligence which takes into	14%	9%	14%	13%

account all human rights (including environment)"				

- **Estimated costs for environmental due diligence**

Most respondents did not provide estimates for required person-days and costs associated with environmental DD. The low response rate may be attributed to the fact that environmental DD was viewed by many respondents as being included in their existing or anticipated DD activities, of which the estimated costs were discussed above. Survey responses indicated that environmental and climate change due diligence is currently usually not undertaken as a standalone process, but that it often takes place in different teams from the human rights and environmental due diligence work. Moreover, survey respondents also indicated that free-standing climate change due diligence is a rather new concept of which many companies are not yet familiar with. Accordingly, we received very limited differentiated information from businesses in this respect.

Only five companies that exclusively undertake environmental and climate change due diligence (not including other human rights issues) provided person-day estimates for environmental and climate change DD (see Table 8.28). Of these, three were companies with 1,000 or more employees, one company with 50 to 249 employees and one company with 250-500 employees. For those three companies with 1,000 or more employees the numbers show a high level of variation and should be interpreted with caution. One company that exclusively undertakes environmental and climate change due diligence provided total cost estimates for environmental and climate change DD, which amount to 23,000 EUR under the status quo and are expected to rise to 78,000 EUR annually under mandatory DD. Again, due to the low response rate these numbers should be interpreted with caution. In addition, some of these respondents may have added additional DD activities when giving their replies. The numbers should therefore not be taken as proxies for activities exclusively related to environmental and climate change DD.

Table 8.28: Respondents' estimates for environmental and climate change due diligence: person-days and costs

Total estimated person-days (5 company respondents)	Status quo	Voluntary guidelines	Mandatory DD reporting	Mandatory DD throughout value chains
1000+ employees		23	45	56
1000+ employees	12	12		12
50 – 249 employees				
1000+ employees	2	436		
250 - 500 employees	7			

Total estimated annual	Status	Voluntary	Mandatory	Mandatory DD

costs in EUR (1 company respondent)	quo	guidelines	DD reporting	throughout value chains
1000+ employees	23,000	56,000	45,000	78,000

Source: Business and Stakeholder Surveys.

- **Estimation of firm-level cost for EU businesses**

Assumptions

The following estimations are based on person-day estimates provided by the respondents to the business stakeholder survey. The person-day estimates reflect companies additional labour costs compared to the status quo, i.e. no policy change. In addition to internal labour cost, we also consider overhead and, based on estimates given by the survey respondents, additional costs resulting from outsourced activities such as external audits.

It should be noted that the person-day estimates provided by the respondents do not fully account for future legal developments (unilateral measures) in the EU's Member States. The survey replies indicate that respondents did not account for potential additional cost resulting from increased regulatory fragmentation in the EU. Generally, divergence in regulatory frameworks across the EU causes additional costs for businesses and impedes intra-EU trade and investment. For DD regulations, the costs of the baseline scenario, i.e. no EU action, would imply considerable additional costs for businesses that trade and/or invest across EU borders if the Member States would enact national DD laws. Accordingly, it would be increasingly difficult for EU companies (who operate different EU markets, as indicated by many survey respondents) to adapt to different legal frameworks in different EU countries, resulting in increased costs. These costs would also impact on the costs of other policy options. Since most EU Member States have not yet adopted national DD laws, we only focus on the cost impact resulting of the proposed policy options for the EU aggregate, i.e. we do not incorporate the cost impact of increasing regulatory fragmentation within the EU. However, compared to fully harmonised EU regulation we expect the additional cost to be significantly higher if companies would have to comply with 28 national laws for which different DD obligations and reporting requirements apply. Assuming that applicable DD obligations, e.g. on-site visits, internal and external audits and mitigation activities, would largely be the same for all 28 EU Member States, the additional cost would mainly result from compliance with national reporting requirements. An EU Directive, i.e. mere minimum standards for DD obligations for the Member States, would also result in additional cost for businesses. An EU Directive would also bear the risk of gold-plating, i.e. over-implementation at national level, which can result in additional costs for businesses.

The estimates presented below represent companies' recurrent costs (over the long-term). The survey respondents did not indicate initial costs (short-term costs), e.g. for hiring staff, the set-up of IT solutions, or initial risk assessments. As outlined in the literature review underlying this report, impact assessments of similar regulations (e.g. the EU Conflict Minerals Regulation and the EU Non-financial Reporting Directive) provide only rudimentary information about initial costs for certain activities or total initial costs. For the EU's Conflict Minerals Regulations, the total initial cost is estimated to amount to 13,500 EUR for companies affected by the regulation. For the EU's Non-financial

Reporting Directive, initial "training" costs are estimated to amount to up to 5,000 EUR. For comprehensive and thus far-reaching DD regulations, we expect the initial cost for businesses to be higher, comprising of costs for staff, training, IT and initial risk assessments conducted either internally or though external parties.

Due to the lack of available data, it is not possible to estimate these costs without having to make highly simplified assumptions for businesses operating in different sectors, companies with different business models and businesses of different sizes. Due to the lack of data and the rather broad definition of the policy options, we do not provide estimates for initial costs. However, these costs should be considered "investment" by businesses to ensure the sustainable operation of the company itself as harm caused to humans and the environment can result in reputational risk affecting the value of the company. To ease the transitional financial burden for businesses, a phase-in period should allow businesses enough flexibilities in terms of time and financial investment. Once specific measures have been proposed by EU lawmakers, businesses should be consulted regarding the length of transitional periods for large businesses and SMEs.

We provide a differentiated picture about the quantitative cost impacts at firm-level for large companies (with more than 250 employees) and SMEs (with up to 249 employees). Based on Eurostat data for the number of enterprises in the EU and size classes, we take into account all EU-based businesses with

- 0-9 employees,
- 10-19 employees,
- 20-49 employees,
- 50-249 employees and
- more than 250 employees (large businesses).

The quantifications are based on person-day estimates that were given by the business stakeholder respondents (for an overview, see Table 8.31 and Table 8.32 below), Eurostat data for the size, revenues and number of enterprises in the EU (according to NACE classifications, level 1; see Table 8.29), and labour cost data provided by Eurostat (see Table 8.30).

We take into account the following goods and services sectors for which reliable firm size data and revenue data as well as the number of firms are provided by Eurostat: Mining and quarrying; Manufacturing; Electricity, gas, steam and air conditioning supply; Construction; Wholesale and retail trade; repair of motor vehicles and motorcycles; Transportation and storage; Accommodation and food service activities; Information and communication; Real estate activities, Professional, scientific and technical activities, Administrative and support service activities. For sub-option 4.1, we also cover companies that operate in mining and extraction industries, textile industries and companies trading and manufacturing food products and agricultural commodities (at NACE level 3). For the EU28, the number of companies by sector and size class is outlined by Table 8.29.

Table 8.29: Number of enterprises in the EU28, by size class

Sector	Number of employees	Eurostat classification	Number of enterprises in 2016 (most recent data)
B Mining and quarrying	0-9	Micro enterprise	14,752
B Mining and quarrying	10-19	Small enterprise	2,100
B Mining and quarrying	20-49	Small enterprise	1,400
B Mining and quarrying	50-249	Medium-sized enterprise	700
B Mining and quarrying	GE250	Large enterprise	223
C Manufacturing	0-9	Micro enterprise	1,750,865
C Manufacturing	10-19	Small enterprise	171,346
C Manufacturing	20-49	Small enterprise	110,000
C Manufacturing	50-249	Medium-sized enterprise	71,921
C Manufacturing	GE250	Large enterprise	16,100
D Electricity, gas, steam and air conditioning supply	0-9	Micro enterprise	105,000
D Electricity, gas, steam and air conditioning supply	10-19	Small enterprise	1,810
D Electricity, gas, steam and air conditioning supply	20-49	Small enterprise	1,504
D Electricity, gas, steam and air conditioning supply	50-249	Medium-sized enterprise	1,412
D Electricity, gas, steam and air conditioning supply	GE250	Large enterprise	607
F Construction	0-9	Micro enterprise	3,307,408
F Construction	10-19	Small enterprise	130,928
F Construction	20-49	Small enterprise	54,817
F Construction	50-249	Medium-sized enterprise	17,511
F Construction	GE250	Large enterprise	1,903
G Wholesale and retail trade; repair of motor vehicles and motorcycles	0_1	Micro enterprise	3,534,931
G Wholesale and retail trade; repair of motor vehicles and motorcycles	10-19	Small enterprise	242,458
G Wholesale and retail trade; repair of motor vehicles and motorcycles	2-9	Micro enterprise	2,367,119

G Wholesale and retail trade; repair of motor vehicles and motorcycles	20-49	Small enterprise	118,678
G Wholesale and retail trade; repair of motor vehicles and motorcycles	50-249	Medium-sized enterprise	45,376
G Wholesale and retail trade; repair of motor vehicles and motorcycles	GE250	Large enterprise	7,848
H Transportation and storage	0_1	Micro enterprise	732,068
H Transportation and storage	10-19	Small enterprise	57,216
H Transportation and storage	2-9	Micro enterprise	
H Transportation and storage	20-49	Small enterprise	37,000
H Transportation and storage	50-249	Medium-sized enterprise	18,300
H Transportation and storage	GE250	Large enterprise	3,637
I Accommodation and food service activities	0_1	Micro enterprise	767,563
I Accommodation and food service activities	10-19	Small enterprise	140,000
I Accommodation and food service activities	2-9	Micro enterprise	1,008,888
I Accommodation and food service activities	20-49	Small enterprise	60,000
I Accommodation and food service activities	50-249	Medium-sized enterprise	16,915
I Accommodation and food service activities	GE250	Large enterprise	1,966
J Information and communication	0_1	Micro enterprise	800,000
J Information and communication	10-19	Small enterprise	
J Information and communication	2-9	Micro enterprise	290,000
J Information and communication	20-49	Small enterprise	
J Information and communication	50-249	Medium-sized enterprise	11,831
J Information and communication	GE250	Large enterprise	2,571
L Real estate activities	0_1	Micro enterprise	1,100,000
L Real estate activities	10-19	Small enterprise	17,178
L Real estate activities	2-9	Micro enterprise	329,351
L Real estate activities	20-49	Small enterprise	7,416
L Real estate activities	50-249	Medium-sized enterprise	3,345
L Real estate activities	GE250	Large enterprise	600
M Professional, scientific and technical activities	0_1	Micro enterprise	3,387,499

M Professional, scientific and technical activities	10-19	Small enterprise	90,840
M Professional, scientific and technical activities	2-9	Micro enterprise	1,049,545
M Professional, scientific and technical activities	20-49	Small enterprise	41,000
M Professional, scientific and technical activities	50-249	Medium-sized enterprise	16,807
M Professional, scientific and technical activities	GE250	Large enterprise	3,000
N Administrative and support service activities	0_1	Micro enterprise	1,029,442
N Administrative and support service activities	10-19	Small enterprise	57,692
N Administrative and support service activities	2-9	Micro enterprise	443,380
N Administrative and support service activities	20-49	Small enterprise	38,666
N Administrative and support service activities	50-249	Medium-sized enterprise	25,529
N Administrative and support service activities	GE250	Large enterprise	6,940

Table 8.30: Labour costs per hour in EUR, annual data of 2018

European Union - 28 countries	**27.4**
Euro area (19 countries)	30.6
Belgium	39.7
Bulgaria	5.4
Czechia	12.6
Denmark	43.5
Germany (until 1990 former territory of the FRG)	34.6
Estonia	12.4
Ireland	32.1
Greece	16.1
Spain	21.4
France	35.8
Croatia	10.9
Italy	28.2

Cyprus	16.3
Latvia	9.3
Lithuania	9
Luxembourg	40.6
Hungary	9.2
Malta	14.7
Netherlands	35.9
Austria	34
Poland	10.1
Portugal	14.2
Romania	6.8
Slovenia	18.1
Slovakia	11.6
Finland	33.6
Sweden	36.6
United Kingdom	27.4

Source: Eurostat.

Note: This table contains data on Average hourly labour costs which are defined as total labour costs divided by the corresponding number of hours worked by the yearly average number of employees, expressed in full-time units. Labour costs cover wages and salaries and non-wage costs (employers' social contributions plus taxes less subsidies).

In related impact assessments, e.g. the EU Non-financial Reporting Directive and the EU Conflict Minerals Regulations, cost estimates were also either taken from the companies' replies gathered through consultations and surveys or estimated by multiplying a given number of working hours (person-days) required (usually stated by the business respondents) and labour costs per hour (usually based on available industry intelligence or publicly available statistics), depending on the administrative procedures prescribed by the intended regulation. We follow a similar methodology. Our estimations are based on person-day estimates that were provided by business respondents. At the same time, as outlined above, many business respondents did not indicate person-day or cost estimates for certain DD activities. Many respondents indicated "No experience" with DD activities. Accordingly, we consider replies from businesses that already conduct certain DD activities most relevant. Of all businesses that provided estimates, the estimates provided by the following groups of respondents are considered most relevant:

- companies with 1,000+ employees that already conduct "Human rights due diligence which takes into account all human rights (including environment)" and
- companies with 50-1,000 employees that already conduct "Human rights due diligence which takes into account all human rights (including environment)".

We at the same time note that these person-day estimates should be interpreted with caution (relevant remarks have also been made in the introductory part of this section):

- In practice, the person-day requirements for information gathering and DD activities vary considerably from company to company, depending on firm and sector characteristics.
- The policy options outlined to the survey respondents are defined in a very broad way. Contrary to other legal proposals, the vague outline of potential DD-related policies leaves a considerable scope of for interpretation and respondents' expectations regarding the potential impacts.
- Some respondents, e.g. CSR managers, may not have had the time to discuss potential cost impacts internally, i.e. checking back with their HR and corporate controlling departments.

Therefore, the estimations provided below should be taken as an indication of general patterns and trends with respect to the escalation of legal obligations and different sizes of companies. At the same time, as will be outlined below, the numbers stated by the respondents are broadly in line with the findings of the impact assessment conducted for related policy measures, e.g. the EU's Non-financial Reporting Directive.

The following estimations are based on an approximation of the survey respondents' estimates and firm-level revenue data provided by Eurostat.

Table 8.31 and Table 8.32 provide a generic (exemplary) overview of the methodology applied to large companies with more than 250 employees and SMEs with up to 249 employees.

For all large companies with more than 250 employees, which are considered "large companies" by Eurostat, we apply estimates that were given by the respondents from companies with 1,000+ employees that already conduct "Human rights due diligence which takes into account all human rights (including environment)" (Table 8.31).

These businesses turn out to be very large in terms of their annual revenues and can be assumed to operate numerous complex value chains. The median annual revenue of those companies the provided estimates is 11.5 billion EUR. To account for size effects among large companies, we scaled the person-day estimates according to companies' revenues, whereby we assume that the median value of the person-day estimates provided by the respondents corresponds to their median revenue of 11.5 billion EUR. According to the estimates provided by the respondents, we assume no change in the required person-days from a shift from the "Status-quo" to "New voluntary measures".[1371]

As outlined in Table 8.31, the number of required person-days would increase moderately from a policy shift from the "status-quo" to "New reporting requirements"

[1371] As outlined above, the slight decrease in the number of required person-days for "New voluntary guidelines" results from differences in the respondents: some respondents who proved estimates for the "Status quo" did not provide estimates for "New voluntary guidelines" and vice versa (see Figure 8.3).

and substantially increase from a policy shift from the "status-quo" to "Mandatory DD throughout companies' value chains". For the group of large companies, we assume the change in required person-days to be proportional to the size of companies' revenues. We consider the size of revenue a more appropriate proxy for value chain length/complexity than the number of employees.

To translate person-days to cost equivalents, we apply the average EU labour cost for a person-day of 8 hours, i.e. 219.20 EUR (27.40 EUR per hour). It should be noted that many large companies have their corporate headquarters and operations in multiple EU and non-EU countries, in which wage levels are relatively high. These companies may face higher labour costs than companies whose headquarters or operations are based in low-wage Member States. The estimated costs resulting from person-day estimates and country-specific labour costs, as outlined above, may therefore underestimate the internal labour costs of companies that are headquartered in EU Member States where salaries are relatively high (and vice versa).

Table 8.31: Firm-level cost based on revenues approximation: large companies with more than 250 employees

Large companies with more than 250 employees: revenue approximation	Baseline: empirical person-days, per month		
Monthly person-days	**Large companies with revenues of 11.5 billion EUR (empirical median)**	**Large companies with revenues of 1 billion EUR**	**Large companies with revenues of 100 million EUR**
Status quo	52	5	0.5
∆ New voluntary guidelines	no change	no change	no change
∆ New reporting requirements	+17	+1	+0
∆ Mandatory DD throughout value chains	+219	+19	+2
	Annual person-day equivalents		
Annual person-days	**Large companies with revenues of 11.5 billion EUR**	**Large companies with revenues of 1 billion EUR**	**Large companies with revenues of 100 million EUR**
Status quo	624	54	5
∆ New voluntary guidelines	no change	no change	no change
∆ New reporting requirements	+204	+18	+2

▵ Mandatory DD throughout value chains	+2,628	+229	+23
	Annual cost (based on EU average hourly labour cost of 27.40 EUR)		
Annual cost equivalents	**Large companies with revenues of 11.5 billion EUR**	**Large companies with revenues of 1 billion EUR**	**Large companies with revenues of 100 million EUR**
Status quo	EUR 136,781	EUR 11,894	EUR 1,189
▵ New voluntary guidelines	no change	no change	no change
▵ New reporting requirements	EUR +44,717	EUR +3,888	EUR +389
▵ Mandatory DD throughout value chains	EUR +576,058	EUR +50,092	EUR +5,009

Source: Own approximations based on Business and Stakeholder Surveys.

For companies with up to 249 employees, which are considered “SMEs” (including micro businesses) by Eurostat, we apply estimates that were given by the respondents from companies with 50-1,000 employees that already conduct “Human rights due diligence which takes into account all human rights (including environment)” (Table 8.32). We applied the same methodology as for large companies. However, the revenues of companies with 50-1,000 employees are much lower than those of companies with 1,000 employees. The median annual revenue of those companies the provided estimates is 128 million EUR. To account for size effects among SMEs, we scaled the person-day estimates according to companies’ revenues, whereby we assume that the median value of the person-day estimates provided by the respondents from companies with 50-1,000 employees corresponds to their median revenue of 128 million EUR. According to the estimates provided by the respondents, we assume no significant change in the required person-days from a shift from the “Status-quo” to “New voluntary measures”.[1372]

Table 8.32: Firm-level cost based on revenues approximation: companies with up to 249 employees

Companies with up to 249 employees: revenue approximation	**Baseline: empirical person-days, per month**		
Monthly person-days	**Companies with revenues of 128**	**Companies with revenues of 10**	**Companies with revenues of 1**

[1372] As outlined above, the respondents only report a slight increase in the number of required person-days for “New voluntary guidelines” (see Figure 8.4).

	million EUR (empirical median)	million EUR	million EUR
Status quo	35	3	0.3
▵ New voluntary guidelines	no change	no change	no change
▵ New reporting requirements	+4	+0.3	+0.0
▵ Mandatory DD throughout value chains	+36	+2.8	+0.3
	Annual person-day equivalents		
Annual person-days	**Companies with revenues of 128 million EUR**	**Companies with revenues of 10 million EUR**	**Companies with revenues of 1 million EUR**
Status quo	420	33	3
▵ New voluntary guidelines	no change	no change	no change
▵ New reporting requirements	+48	+4	+0.4
▵ Mandatory DD throughout value chains	+432	+34	+3.4
	Annual cost (based on EU average hourly labour cost of 27.4 EUR)		
Annual cost equivalents	**Companies with revenues of 128 million EUR**	**Companies with revenues of 10 million EUR**	**Companies with revenues of 1 million EUR**
Status quo	EUR 92,064	EUR 7,193	EUR 719
▵ New voluntary guidelines	no change	no change	no change
▵ New reporting requirements	EUR +10,522	EUR +822	EUR +82
▵ Mandatory DD throughout value chains	EUR +94,694	EUR +7,398	EUR +740

Source: Own approximations based on Business and Stakeholder Surveys.

It should be noted that the applied methodology, which differentiates between large companies and SMEs, has some limitations. Due to the lack of available data, the methodology, i.e. the approximation, causes in a structural break in the estimates for companies with revenues with more/less than 128 million EUR. Eurostat data is only available for large companies with more than 250 employees and SMEs with up to 249 employees. Accordingly, the structural break affects some large companies (in terms of employees) with relatively low revenues and some companies that have less than 250 employees, but relatively high revenues. At the same time, it should be noted that, due to the implementation of efficient DD procedures, e.g. by use of modern tracking technologies, some SMEs may face lower relative cost than large companies. The actual impact depends on the complexity of the value chains and the scope for exploitation of potential economies of scale, while large companies generally perform better in exploiting potential economies of scale than SMEs.

However, we consider the numbers for smaller companies more appropriate than assuming a linear relationship for all companies. First, applying the estimates that were given by respondents from very large companies would result in very low, often negligible results for many SMEs, particularly very small SMEs in terms of their annual revenues. Second, accounting for a non-linear relationship between company size and person-days requirements for large companies and SMEs recognises that large companies benefit from economies of scale in various respects, e.g. a wide range of existing DD activities, existing man-power specialised in value chain management, existing technological solutions not available to SMEs. Our approximations indicate that, compared to large companies, the cost-revenue ratio is 21 times higher for SME for new reporting requirements and 15 times higher for SMEs for mandatory DD. These numbers should not be taken by face value. These numbers are the result of our approximation and reflect a general pattern. A company's ability to benefit from economies of scale critically depends on firm and sector characteristics.

At the same time, as concerns the additional recurrent firm-level costs as percentages of companies' revenues, these numbers could be interpreted as ad valorem tariff equivalents (AVEs), which are relatively low compared to applied tariffs on goods imports to the EU or exports from the EU (in 2017 the weighted mean average tariff of the EU was 1.8%, while peak tariffs are substantially higher for certain product categories, e.g. agricultural commodities). Nevertheless, for companies that would have to rearrange their value chains and relocate certain production activities to countries/regions with lower human rights and environmental risks, there would be an additional initial cost burden (divestment in high-risk countries; investment in low-risks countries) that would be substantially higher than the recurrent costs, which are mainly staff-driven.

The numbers of this estimation should also be put into perspective with estimates outlined in the impact assessment of the EU Non-Financial Reporting Directive, which finds that large companies' additional annual costs amount to 155,000 and 604,000 EUR, while SMEs additional cost are substantially lower, amounting to 8,000 and 25,000 EUR (Table 0.1 of Part IV: Annexures). It should be noted that the "New reporting requirements" would go beyond the reporting requirements of the Non-financial Reporting Directive, while new "Mandatory DD" would add substantial additional information and mitigation requirements to companies' value chain management, reporting and general DD activities, resulting in significantly higher additional costs.

Table 8.33: Additional firm-level cost as percentages of revenues, large companies vs. SMEs

	New voluntary guidelines	New reporting requirements	Mandatory DD throughout value chains
Large companies (based on revenues approximation; baseline:	no change	0.0004%	0.0050%

annual revenue of 11.5 billion EUR)			
SMEs (based on revenues approximation; baseline: annual revenue of 128 billion EUR)	no change	0.0082%	0.0740%
Economies of scale factor large companies / SMEs		0.0473	0.0677
Economies of scale factor SMEs / large companies		21	15

Source: Own approximations based on Business and Stakeholder Surveys.

Taking into account the additional burden, we consider our results to be in line with the findings of the impact assessment for the EU's Non-financial Reporting Directive. For mandatory DD, for example, our estimates indicate that a representative large company with revenues of 10 billion EUR would face additional annual labour cost of approximately 500,920 EUR. By comparison, for mandatory DD, our estimates indicate that a representative SME with revenues of 1 million EUR would face additional annual labour cost of approximately 740 EUR, while a large SME with annual revenues of 50 million EUR (the upper bound according the Eurostat SME definitions) would face additional annual labour cost of 36,990 EUR (see Table 8.34).

The estimates nevertheless represent averages across companies from all sectors of the economy. Depending on companies' business model, value chain complexities and the degree of internationalisation, the numbers can be substantially lower or higher for some businesses. For example, depending on the final regulations the recurrent costs may be much more significant for the financial sector than for other companies. This is because of the financial sector's role in financing and facilitating the economic activities of companies in just about any other sector of the economy. Similarly, for companies that are engaged in online intermediation (mainly for physical goods) or physical retail services, the costs may also be more substantial than for companies that produce and market only a low number of products and services, with a low number of suppliers/business partners respectively.

Table 8.34: Overview of estimated additional labour cost excl. overhead and cost of outsourced activities / audits, large companies vs. SMEs

Large companies			
Revenue	**▵ New voluntary guidelines**	**▵ New reporting requirements**	**▵ Mandatory DD throughout value chains**
EUR 50,000,000,000	no change	EUR 194,420.87	EUR 2,504,598.26
EUR 10,000,000,000	no change	EUR 38,884.17	EUR 500,919.65

EUR 1,000,000,000	no change	EUR 3,888.42	EUR 50,091.97
EUR 100,000,000	no change	EUR 388.84	EUR 5,009.20
SMEs			
Revenue	**∆ New voluntary guidelines**	**∆ New reporting requirements**	**∆ Mandatory DD throughout value chains**
EUR 50,000,000	no change	EUR 4,110	EUR 36,990
EUR 25,000,000	no change	EUR 2,055	EUR 18,495
EUR 10,000,000	no change	EUR 822	EUR 7,398
EUR 1,000,000	no change	EUR 82	EUR 740

Source: Own approximations based on Business and Stakeholder Surveys.

Table 8.35 outlines annual cost estimates including companies' internal labour costs, the costs of overhead and costs of "outsourced activities / audits". We applied a 25% mark-up for overhead relative to labour costs (expenses not related to direct labour, e.g. the cost of office equipment, rent and personnel administration).[1373] Empirical mark-ups for "outsourced activities / audits" have been taken from the survey replies. For "New reporting requirements", we applied a 17% mark-up on the estimated additional labour costs. For "Mandatory DD", we applied a 25% mark-up on the estimated additional labour costs (see Table 8.27).

Table 8.35: Overview of estimated additional labour cost incl. overhead and cost of outsourced activities / audits, large companies vs. SMEs

Large companies			
Revenue	**∆ New voluntary guidelines**	**∆ New reporting requirements**	**∆ Mandatory DD throughout value chains**
EUR 50,000,000,000	no change	EUR 345,097.04	EUR 4,696,121.74
EUR 10,000,000,000	no change	EUR 69,019.41	EUR 939,224.35
EUR 1,000,000,000	no change	EUR 6,901.94	EUR 93,922.43
EUR 100,000,000	no change	EUR 690.19	EUR 9,392.24
SMEs			

[1373] Businesses have regular expenses that are not directly related to producing goods or services. These indirect costs are termed "overhead". Most businesses calculate overhead costs on a monthly basis. Typically, overhead is expressed as a percentage of sales or labour cost. The 25% mark-up is also applied in the EU's Horizon funding programmes.

Revenue	∆ New voluntary guidelines	∆ New reporting requirements	∆ Mandatory DD throughout value chains
EUR 50,000,000	no change	EUR 7,295.25	EUR 69,356.25
EUR 25,000,000	no change	EUR 3,647.63	EUR 34,678.13
EUR 10,000,000	no change	EUR 1,459.05	EUR 13,871.25
EUR 1,000,000	no change	EUR 145.91	EUR 1,387.13

Source: Own approximations based on Business and Stakeholder Surveys. Note: we applied a 25% mark-up for overhead relative to labour costs. For "New reporting requirements", we applied a 17% mark-up on the estimated additional labour costs. For "Mandatory DD", we applied a 25% mark-up on the estimated additional labour costs (see Table 8.27).

Aggregate firm-level costs across policy options

For the EU as a whole, Table 8.36 provides an overview of the additional aggregate firm-level cost that would result from the proposed policy option. The estimates are based on the revenues of EU enterprises for different sectors and size classes, for which the data is provided in Table 0.2 of Part IV: Annexures. The numbers represent total annual cost estimates for large companies and SMEs. If new regulation would be applied horizontally across the EU, EU companies' additional cost would be highest for policy option 4 requiring "Mandatory DD throughout companies' value chains", amounting to about 33 billion EUR annually. For policy option 3 on "New reporting requirements", EU companies' additional aggregate cost would amount to about 3.5 billion EUR annually.

It should be noted that respondents' data was not clear about the total costs of DD activities resulting from checks and reporting activities concerning 1st-tier suppliers only and whether these estimates also included other suppliers (suppliers of suppliers) along their value chains. Accordingly, the numbers should be read as a lower-bound estimate.

On the other hand, companies that source from the same suppliers may be able to share the costs in the future, e.g. by cooperating in risk assessments or through the purchase of assessments by external audit providers, etc. These overlaps in business relations could result in cost savings. The survey replies indicate that business respondents have not taken into account such savings. This may have resulted in an overestimation of companies' additional recurrent costs.

It should also be noted that in an ideal world, if every (EU) business conducts its own due diligence in accordance with the (EU) law, companies may only incur costs relating to their own impacts and those of relationships outside of the EU. If an EU due diligence law would reduce the practical scope of EU businesses' due diligence activities once they have done their risk assessment this would result in cost reductions.

Table 8.36: Estimated additional firm-level cost, EU aggregate

	Labour cost	Overhead	Cost of outsourced activities / audits	Total additional annual firm-level cost
Option 1: no policy change (baseline scenario)	no change	no change	no change	no change
Option 2: new voluntary guidelines / guidance	no change	no change	no change	no change
Option 3: New regulation requiring due diligence reporting	EUR 2,435,441,525	EUR 608,860,381	EUR 414,025,059	EUR 3,458,326,965
Option 4: New regulation requiring mandatory due diligence as a legal duty of care	EUR 22,028,160,401	EUR 5,507,040,100	EUR 5,507,040,100	EUR 33,042,240,602

Source: Own approximations based on Business and Stakeholder Surveys.

Company-level cost for Option 4: New regulation requiring mandatory DD as legal duty of care

Sub-option 4.1: New regulation applying to a narrow category of business (limited by sector)

Based on the clarifications with the client, we provide cost estimates for EU companies that operate in mining and extraction industries, textile industries and companies trading and manufacturing food products and agricultural commodities. A full list of sectors, which are based on NACE 3 classifications, is provided by Table 8.37. Due to the very high number of sectors and the required differentiation according to company size categories, we only provide aggregate numbers for the EU28 broken down by the three sectors (see Table 8.38). The numbers indicate that, because of its substantial size, the EU's food and agricultural sector would show the highest increase in costs resulting from "New mandatory DD throughout companies' value chains".

As shown by Table 8.38, we estimate the total additional cost for EU companies operating in the mining and extraction industries to amount to up to 42.3 million EUR (6.2 million EUR for large companies and 36 million EUR for SMEs).

The total additional cost for EU companies operating in the textiles industries are estimated to amount up to 110 million EUR per year (3.7 million EUR for large companies and 107 million EUR for SMEs).

The total additional cost for EU companies that trade or manufacture of food products and agricultural commodities amount to up to 2.3 billion EUR annually (56 million EUR for large companies and 2.27 billion EUR for SMEs).

Table 8.37: Overview of sectors: mining and extraction industries, food products and agricultural commodities, textile industries – NACE Level 3

Mining and extraction industries	Total costs trade and manufacturing of food products and agricultural commodities	Textile industries
B051 Mining of hard coal	C101 Processing and preserving of meat and production of meat products	C131 Preparation and spinning of textile fibres
B051 Mining of hard coal	C101 Processing and preserving of meat and production of meat products	C131 Preparation and spinning of textile fibres
B051 Mining of hard coal	C101 Processing and preserving of meat and production of meat products	C131 Preparation and spinning of textile fibres
B051 Mining of hard coal	C101 Processing and preserving of meat and production of meat products	C131 Preparation and spinning of textile fibres
B051 Mining of hard coal	C101 Processing and preserving of meat and production of meat products	C131 Preparation and spinning of textile fibres
B052 Mining of lignite	C102 Processing and preserving of fish, crustaceans and molluscs	C132 Weaving of textiles
B052 Mining of lignite	C102 Processing and preserving of fish, crustaceans and molluscs	C132 Weaving of textiles
B052 Mining of lignite	C102 Processing and preserving of fish, crustaceans and molluscs	C132 Weaving of textiles
B052 Mining of lignite	C102 Processing and preserving of fish, crustaceans and molluscs	C132 Weaving of textiles
B052 Mining of lignite	C102 Processing and preserving of fish, crustaceans and molluscs	C132 Weaving of textiles
B061 Extraction of crude petroleum	C103 Processing and preserving of fruit and vegetables	C133 Finishing of textiles
B061 Extraction of crude petroleum	C103 Processing and preserving of fruit and vegetables	C133 Finishing of textiles
B061 Extraction of crude petroleum	C103 Processing and preserving of fruit and vegetables	C133 Finishing of textiles
B061 Extraction of crude petroleum	C103 Processing and preserving of fruit and vegetables	C133 Finishing of textiles
B061 Extraction of crude	C103 Processing and preserving	C133 Finishing of textiles

Mining and extraction industries	Total costs trade and manufacturing of food products and agricultural commodities	Textile industries
petroleum	of fruit and vegetables	
B062 Extraction of natural gas	C104 Manufacture of vegetable and animal oils and fats	C139 Manufacture of other textiles
B062 Extraction of natural gas	C104 Manufacture of vegetable and animal oils and fats	C139 Manufacture of other textiles
B062 Extraction of natural gas	C104 Manufacture of vegetable and animal oils and fats	C139 Manufacture of other textiles
B062 Extraction of natural gas	C104 Manufacture of vegetable and animal oils and fats	C139 Manufacture of other textiles
B062 Extraction of natural gas	C104 Manufacture of vegetable and animal oils and fats	C139 Manufacture of other textiles
B071 Mining of iron ores	C105 Manufacture of dairy products	C141 Manufacture of wearing apparel, except fur apparel
B071 Mining of iron ores	C105 Manufacture of dairy products	C141 Manufacture of wearing apparel, except fur apparel
B071 Mining of iron ores	C105 Manufacture of dairy products	C141 Manufacture of wearing apparel, except fur apparel
B071 Mining of iron ores	C105 Manufacture of dairy products	C141 Manufacture of wearing apparel, except fur apparel
B071 Mining of iron ores	C105 Manufacture of dairy products	C141 Manufacture of wearing apparel, except fur apparel
B072 Mining of non-ferrous metal ores	C106 Manufacture of grain mill products, starches and starch products	C142 Manufacture of articles of fur
B072 Mining of non-ferrous metal ores	C106 Manufacture of grain mill products, starches and starch products	C142 Manufacture of articles of fur
B072 Mining of non-ferrous metal ores	C106 Manufacture of grain mill products, starches and starch products	C142 Manufacture of articles of fur
B072 Mining of non-ferrous metal ores	C106 Manufacture of grain mill products, starches and starch products	C142 Manufacture of articles of fur
B072 Mining of non-ferrous metal ores	C106 Manufacture of grain mill products, starches and starch products	C142 Manufacture of articles of fur

Mining and extraction industries	Total costs trade and manufacturing of food products and agricultural commodities	Textile industries
B081 Quarrying of stone, sand and clay	C107 Manufacture of bakery and farinaceous products	C143 Manufacture of knitted and crocheted apparel
B081 Quarrying of stone, sand and clay	C107 Manufacture of bakery and farinaceous products	C143 Manufacture of knitted and crocheted apparel
B081 Quarrying of stone, sand and clay	C107 Manufacture of bakery and farinaceous products	C143 Manufacture of knitted and crocheted apparel
B081 Quarrying of stone, sand and clay	C107 Manufacture of bakery and farinaceous products	C143 Manufacture of knitted and crocheted apparel
B081 Quarrying of stone, sand and clay	C107 Manufacture of bakery and farinaceous products	C143 Manufacture of knitted and crocheted apparel
B089 Mining and quarrying n.e.c.	C108 Manufacture of other food products	C151 Tanning and dressing of leather; manufacture of luggage, handbags, saddlery and harness; dressing and dyeing of fur
B089 Mining and quarrying n.e.c.	C108 Manufacture of other food products	C151 Tanning and dressing of leather; manufacture of luggage, handbags, saddlery and harness; dressing and dyeing of fur
B089 Mining and quarrying n.e.c.	C108 Manufacture of other food products	C151 Tanning and dressing of leather; manufacture of luggage, handbags, saddlery and harness; dressing and dyeing of fur
B089 Mining and quarrying n.e.c.	C108 Manufacture of other food products	C151 Tanning and dressing of leather; manufacture of luggage, handbags, saddlery and harness; dressing and dyeing of fur
B089 Mining and quarrying n.e.c.	C108 Manufacture of other food products	C151 Tanning and dressing of leather; manufacture of luggage, handbags, saddlery and harness; dressing and dyeing of fur
B091 Support activities for petroleum and natural gas extraction	C109 Manufacture of prepared animal feeds	C152 Manufacture of footwear
B091 Support activities for petroleum and natural gas extraction	C109 Manufacture of prepared animal feeds	C152 Manufacture of footwear
B091 Support activities for petroleum and natural gas extraction	C109 Manufacture of prepared animal feeds	C152 Manufacture of footwear

Mining and extraction industries	Total costs trade and manufacturing of food products and agricultural commodities	Textile industries
B091 Support activities for petroleum and natural gas extraction	C109 Manufacture of prepared animal feeds	C152 Manufacture of footwear
B091 Support activities for petroleum and natural gas extraction	C109 Manufacture of prepared animal feeds	C152 Manufacture of footwear
B099 Support activities for other mining and quarrying	C110 Manufacture of beverages	
B099 Support activities for other mining and quarrying	C110 Manufacture of beverages	
B099 Support activities for other mining and quarrying	C110 Manufacture of beverages	
B099 Support activities for other mining and quarrying	C110 Manufacture of beverages	
B099 Support activities for other mining and quarrying	C110 Manufacture of beverages	
	C120 Manufacture of tobacco products	
	C120 Manufacture of tobacco products	
	C120 Manufacture of tobacco products	
	C120 Manufacture of tobacco products	
	C120 Manufacture of tobacco products	
	G462 Wholesale of agricultural raw materials and live animals	
	G462 Wholesale of agricultural raw materials and live animals	
	G462 Wholesale of agricultural raw materials and live animals	
	G462 Wholesale of agricultural raw materials and live animals	
	G462 Wholesale of agricultural	

Mining and extraction industries	Total costs trade and manufacturing of food products and agricultural commodities	Textile industries
	raw materials and live animals	
	G462 Wholesale of agricultural raw materials and live animals	
	G463 Wholesale of food, beverages and tobacco	
	G463 Wholesale of food, beverages and tobacco	
	G463 Wholesale of food, beverages and tobacco	
	G463 Wholesale of food, beverages and tobacco	
	G463 Wholesale of food, beverages and tobacco	
	G463 Wholesale of food, beverages and tobacco	
	G472 Retail sale of food, beverages and tobacco in specialised stores	
	G472 Retail sale of food, beverages and tobacco in specialised stores	
	G472 Retail sale of food, beverages and tobacco in specialised stores	
	G472 Retail sale of food, beverages and tobacco in specialised stores	
	G472 Retail sale of food, beverages and tobacco in specialised stores	
	G472 Retail sale of food, beverages and tobacco in specialised stores	

Source: Own selection based on Eurostat classifications.

Table 8.38: Total of annual firm-level costs for Sub-option 4.1: mining and extraction industries, food products and agricultural commodities, textile industries, EU aggregates

Sector	Labour cost	Overhead	Cost of outsourced activities / audits	Total additional annual firm-level cost
Large companies				
Mining and extraction	EUR 4,401,321	EUR 1,100,330	EUR 748,224	**EUR 6,249,875**
Textiles	EUR 2,452,523	EUR 613,131	EUR 613,131	**EUR 3,678,784**
Trade and manufacturing of food products and agricultural commodities	EUR 39,476,090	EUR 9,869,023	EUR 6,710,935	**EUR 56,056,048**
SMEs				
Mining and extraction	EUR 24,007,028	EUR 6,001,757	EUR 6,001,757	**EUR 36,010,542**
Textiles	EUR 75,188,093	EUR 18,797,023	EUR 12,781,976	**EUR 106,767,093**
Trade and manufacturing of food products and agricultural commodities	EUR 1,514,112,336	EUR 378,528,084	EUR 378,528,084	**EUR 2,271,168,504**
TOTAL	**EUR 1,659,637,390**	**EUR 414,909,348**	**EUR 405,384,107**	**EUR 2,479,930,845**

Source: Own calculations based on Business and Stakeholder Surveys. Note: we applied a 25% mark-up for overhead relative to labour costs. For "New reporting requirements", we applied a 17% mark-up on the estimated additional labour costs. For "Mandatory DD", we applied a 25% mark-up on the estimated additional labour costs (see Table 8.27).

Sub-option 4.2: New regulation applying horizontally across sectors

Sub-option 4.2(a): applying only to a defined set of large companies

Large companies' additional cost would be highest for policy option 4 requiring "Mandatory DD throughout companies' value chains", amounting to about 543 million EUR. For policy option 3 on "New reporting requirements", EU companies' additional aggregate cost would amount to about 40 million EUR annually (see also Table 8.36).

Sub-option 4.2(b): applying to all business, including SMEs

If new regulation would be applied horizontally across the EU, EU companies' additional cost would be highest for policy option 4 requiring "Mandatory DD throughout companies' value chains", amounting to about 33 billion EUR annually. For policy option 3 on "New reporting requirements", EU companies' additional aggregate cost would amount to about 3.5 billion EUR annually (see also Table 8.36).

It should be noted that SMEs costs could disproportionately rise, particularly for small companies operating in retail and wholesale trading or the manufacturing sector as these sectors that are generally characterised by complex and often international value chains. In addition, compared to larger companies a reputation-based increase in SMEs total sales is less likely to generate additional income sufficient to cover additional costs that result from new DD requirements.

However, as the findings from elsewhere in this study show, due diligence as a standard of care relatesto what could be reasonably expected of the company in its particular circumstances, risks and operating context. In this way, courts or regulators would take into account what could be reasonably expected of SMEs with small profit margins and low or indirect risks, taking into account the nature of the risks and the SME's leverage efforts. The literature relating to disclosure requirements, which arguably impose disproportionate costs burdens on SMEs who are required to produce reports of similar length and detail as large companies, discuss the risks of SMEs suffering costs and even being drive out of business as a result of transparency regulations. In contrast, the analysis elsewhere in this study imply that a correct application of due diligence as a standard of care should not expect the average micro business to undertake such disproportionately burdensome activity that it drives them out of business. Nevertheless, the introduction of a standard of care may have some impact on the closure of micro companies which have severe risks of their own, or in their value chain which it cannot address through exercising leverage.

- **The impacts on competitiveness, trade and innovation**

The impact on EU companies' competitiveness is difficult to assess ex-ante. Generally, as concerns EU companies' competitiveness within the Single Market, the impact critically depends on whether non-EU companies operating in the EU are affected by the regulations, or whether they are carved-out. If EU DD regulation would only apply for companies that are based in the EU, EU companies would be at a relative disadvantage compared to non-EU importers of goods and services that do not have to comply with any form of DD regulation. Non-EU companies would benefit from relative cost advantages vis-à-vis EU-based companies. Non-EU companies would neither have to bear the recurrent costs for DD activities not the initial cost for investment in staff and IT and/or the relocation of certain production activities to low-risk countries/regions. Accordingly, the least distortions of competition within the EU's Single Market can be expected from a mix of policies that equally affect all companies that operate in the EU.

As concerns EU companies' international cost competitiveness, higher administrative costs and greater legal risks/uncertainties generally decrease EU businesses' competitiveness. If non-EU countries would abstain from the implementation of DD laws, negative impacts for EU businesses would mainly result from policy options 3 and 4. The negative impacts would be highest for policy option 4, which implies the highest administrative cost and at the same time high legal risks, e.g. the risk of sanctions in case of unforeseen (unexpected) human rights infringements in the value chain, which may require a relocation of production activities away from high-risk countries.

EU exports, EU imports and EU investment in non-EU countries

As concerns EU trade flows, we do not expect significant negative distortions for EU exporters that result from increased recurrent administrative cost. Expressed in ad valorem tariff equivalents (AVEs, additional firm-level costs as percentages of companies' revenues), the numbers are relatively low (<0.1%) compared to, for example, the applied average tariff for goods imported to the EU (in 2017 the weighted mean average tariff of the EU was 1.8%). However, we note that our estimates do not include cost for policy-induced rearrangements of companies' value chains, which can be substantial, particularly for with vast production facilities, e.g. manufacturing companies that either operate their own plants or entered into supply agreements with suppliers in high-risk countries. The costs of rearranging value chains and/or the relocation of production would have a negative impact on the international competitiveness of EU exporters. In some cases, a one-time rearrangement/relocation may translate to higher recurrent costs, e.g. when production is relocated to countries/regions with higher wages, higher costs for energy or higher taxes. Increases in recurrent costs would adversely impact on EU companies' medium-to long-term export competitiveness, particularly those companies that import large amount of intermediate products/inputs from low-cost, incl. low-wage, jurisdictions.

Regarding EU imports and EU businesses' investment (FDI) in non-EU countries, some internationally operating companies may have to entirely withdraw from non-EU markets that are relatively risky with respect to human rights and environmental risks and high monitoring and mitigation costs respectively (full disengagement). At the same time, it should be noted that the UNGPs expressly state that DD does not necessarily imply a termination the relationship or leaving the jurisdiction, as this might have negative impacts on the respective regions. Instead, the businesses should exercise leverage to try and improve conditions. In certain cases, it will not be possible to improve, but only if the business was already so harmful that the company cannot have relationships with it anymore, and cannot do anything else about it. This is a last resort and an extreme example, literally described as such by the UNGPs. Accordingly, "forced disengagement" would not be the intended outcome of an EU DD law. Instead, the impact of the law should be to force companies to improve their conditions. If the law applies to the company's global operations, it will in any event not be able to just move elsewhere, as there will be other problems there.

It is not possible to make any precise projections about the number/rate of companies' withdrawals for certain countries and/or industries. Depending on the precise text of the DD obligations, individual companies would have to assess and mitigate risks throughout their operations. These operations, however, take place in countries whose formal and informal institutions are not likely to change in the short-term (e.g. forced labour, unsafe or unhealthy working conditions; discrimination by race, age, gender, sexuality and other protected attributes; underpayment for labour), potentially requiring companies' to reconsider their engagements. Thereby, the rate of withdrawal is likely to be higher for countries that are known for considerably high human rights risks. Table 8.39 exemplarily outlines the bottom-30 countries with the highest human rights risks (as of 2017) and the 2018 value of EU28 goods imports from these countries. It should be noted that, depending on the precise legal provisions, EU exporters (downstream business partners/customers) as well as investors (most likely FDI engagements) could also be affected by a new EU DD regulation.

Lessons from existing instruments

It should be noted that there is only very limited evidence for the impact of related instruments on trade flows between the EU and non-EU countries. There is no evidence so far that the EU's Non-financial Reporting Directive had an impact on trade flows between the EU and third countries. The impacts of the EU Conflict Minerals Regulations remain to be seen. At the same time, for the US Conflict Minerals Regulation recent evidence suggests that the US regulation led to a significant reduction in the number of conflict mines for the 3T minerals in Eastern Congo (Democratic Republic of Congo).[1374] Also, beyond the four conflict minerals (gold, tin, tantalum, tungsten), EU imports of mining products and non-ferrous metals from the Democratic Republic of Congo increased strongly after 2015.[1375] On aggregate, exports of metals and mineral products from the Democratic Republic of Congo also increased significantly since 2013, e.g. cobalt, copper, cobalt ore, copper ore). These developments show that there can be a reallocation of resources in countries with high human rights risks, which, over time, may lead to more production and exports in other sectors of the economy. It should be noted, however, that these effects are different and less likely to take place for sectors where international competition is already strong. For natural resources, the comparative advantage of resource-rich countries is unlikely to erode if international supply remains limited and international demand remains strong.

Table 8.39 Top 30 of countries with greatest human rights risks and EU28 import volumes

Country	Human Rights Protection Scores (by Christopher Farris and Keith Schnakenberg)	Total goods import to the EU28, in million EUR (EURO)
Thailand	(1.209)	22,859
Ukraine	(1.219)	18,017
Russia	(1.232)	168,273
Congo	(1.286)	866
China	(1.299)	394,819
Iran	(1.378)	9,453
India	(1.394)	45,829
Bangladesh	(1.423)	17,850
Mexico	(1.423)	26,029

[1374] Enoughproject (2018), Progress and Challenges on Conflict Minerals: Facts on Dodd-Frank 1502. Available at https://enoughproject.org/special-topics/progress-and-challenges-conflict-minerals-facts-dodd-frank-1502.
[1375] European Commission (2019). European Union, Trade in goods with Congo (Democratic Rep). Available at https://webgate.ec.europa.eu/isdb_results/factsheets/country/details_congo-democratic-rep_en.pdf.

Venezuela	(1.435)	1,688
Egypt	(1.536)	8,503
Pakistan	(1.581)	6,882
Burundi	(1.595)	25
Turkey	(1.620)	76,141
Somalia	(1.739)	24
Ethiopia	(1.950)	652
Eritrea	(1.964)	2
Libya	(1.976)	16,786
Central African Republic	(2.057)	14
Nigeria	(2.059)	22,546
Yemen	(2.108)	40
Philippines	(2.131)	7,936
Afghanistan	(2.311)	28
Iraq	(2.388)	16,353
Democratic Republic of Congo	(2.431)	1,487
North Korea	(2.438)	3
Myanmar	(2.467)	2,295
Sudan	(2.471)	154
Syria	(2.559)	107
South Sudan	(2.592)	0

Source: European Commission (trade volumes) and Harvard Dataverse (human rights protection scores)[1376]

EU companies might also be replaced by companies that do not have to comply with DD regulations, even though some of these companies pose a higher risk of human rights infringements than EU-based companies. As concerns sectors with relatively high human rights risks, we acknowledge that certain industries are frequently in the limelight of civil society and the political debate, e.g. mining, textiles and agriculture. However, we recognise that human rights infringements are not only common in these sectors, with numerous blind spots. Poor working conditions, for example, are also common in

[1376] See Schnakenberg, K. E. & Fariss, C. J. (2014). Dynamic Patterns of Human Rights Practices. Political Science Research and Methods, 2(1), 1–31. doi:10.1017/psrm.2013.15 Fariss, C. J. (2019). Yes, Human Rights Practices Are Improving Over Time. American Political Science Review. Data vailable at https://dataverse.harvard.edu/dataset.xhtml?persistentId=doi:10.7910/DVN/TADPGE.

constructions sectors. A replacement of EU construction businesses operating in African countries by Chinese or Indian competitors may thus result in a worse human rights situation compared to the status quo.

Impact on production and employment in the Single Market

The disengagement effect might have a positive impact on the creation of value added (production) and employment in the EU's Single Market. In addition to direct employment effects resulting from businesses' need to comply with new DD regulations (see FTE estimates outlined in Table 8.56), the relocation of investment to the EU and/or sourcing of inputs to suppliers based in the EU would lead to greater levels of production and employment respectively.

Precise quantitative impacts are, however, difficult to project as they depend on numerous determinants, e.g. different company-specific characteristics, businesses' operations in high-risk jurisdictions, but also EU countries' relative attractiveness for investment in certain sectors of the economy (labour-intensive, vs. knowledge-intensive, energy-intensive), and, after all, the nature of the obligations set out in DD regulations.

Generally, Central and Eastern European (CEE) countries are more likely to benefit from relocation effects. This is due to their relative wage competitiveness vis-à-vis Western European countries and the fact the there is a greater potential for relocation of labour-intensive activities and activities conducted by relatively low-skilled workers.

SMEs and businesses with low profit margins

Due to size advantages, large companies are more likely to remain competitive as the additional cost burden accounts for a much smaller relative share in these companies' total costs. A reputation-induced increase in the sales volumes of larger companies may generate sufficient income to cover the cost of tighter DD regulations. It should be noted that large companies are more likely to see a financial net benefit from reputation-induced increases in sales. Due to their size, a reputation-based increase in total sales is more likely to generate additional income sufficient to cover the additional costs that result from new DD requirements. At the same time, companies with relatively low annual revenues might not be able to compensate higher costs through reputation-induced increases in sales and net income respectively. Moreover, companies with low profit margins would face the risk of being driven out of business as the reputation-induced increase in sales might not generate income sufficient to cover the additional regulation-induced cost burden.

By contrast small companies with low profit margins are more likely to be driven out of business than large companies with low profit margins. Small companies generally find it harder to cover the costs resulting from additional human and administrative resources that are needed to comply with DD regulations. At the same time, as concerns DD obligations, small businesses' burden will entirely depend on the risks of the company. It should also be noted that due diligence is a standard that is based on what could be reasonably expected of the company. The costs for individual SMEs may be lower if they already have established DD practices in place for human rights and environmental impacts.

DD includes a prioritisation exercise based on severity of risks, and acknowledges that SMEs have limited resources. An application whereby a micro business is expected to undertake disproportionately burdensome activities that these activities drive it out of business, would not be a correct interpretation of the standard. The introduction of a standard of care may have some impact on the closure of micro companies which have very severe risks which it cannot address through exercising leverage. Finally, if all companies in the supply chain were to exercise appropriate due diligence, SMEs' costs would be significantly lower as they would mainly need to focus on their own risks.

Factors contributing to greater level of competitiveness include advantages in attracting and retaining employees, greater consumer loyalty, less operational delays, less problematic relations with governments and local communities, and less reputational risks and damages. While it is generally difficult to quantify changes in companies' relative competitiveness, it can be assumed that companies with DD activities in place are more likely to enjoy these benefits. At the same time, the relative size of these benefits vis-à-vis companies without DD procedures in place would erode over time if DD would become mandatory by law.

Recent studies indicate that the globalisation of business and investment activities has increased the demand for more transparent accounting of corporate responsibilities encompassing human rights, social, economic and environmental dimensions. While this trend mainly affects (large) internationally operating companies, a non-level-playing field for businesses of all sizes, incl. SMEs, would still create distortions of competition as companies based in certain jurisdictions would have to comply with DD policies while companies based outside these jurisdictions (e.g. mere importers) would not necessarily be affected be such regulations.

According to the replies of the survey respondents, the greatest number of businesses expecting significant benefits (16%) or very significant benefits (24%) is recorded for Mandatory DD policies compared to New voluntary guidelines and New reporting requirements (see Table 8.40). The outcome suggests that businesses indeed anticipate adverse impacts on their competitiveness due to new DD policies, but at the same time expect least distortions if new EU regulation creates more equal standards for EU & non-EU suppliers. It should also be noted that the percentage share of business respondents expecting significant or very significant benefits is substantially larger for Mandatory DD than for New Reporting requirements and new voluntary guidelines respectively.

Table 8.40 Respondents' replies regarding distortion of competition due to more equal standards for EU & non-EU suppliers

		No benefits	Some benefits	Moderate benefits	Significant benefits	Very significant benefits	Do not know
Option 2: **New voluntary guidelines**	Less distortion of competition due to more equal standards for EU & non-EU suppliers	28.26%	14.13%	20.65%	13.04%	6.52%	17.39%
	Change in percentage points: Option 3 vs. Option 2	-0.35%	-2.50%	2.61%	5.56%	-0.71%	-4.60%
Option 3:	Less distortion of competition	27.91%	11.63%	23.26%	18.60%	5.81%	12.79%

New reporting requirements	due to more equal standards for EU & non-EU suppliers						
	Change in percentage points: Option 34 vs. Option 2	-8.75%	-3.15%	-1.14%	**2.81%**	**17.87%**	-7.63%
Option 4: **Mandatory DD**	Less distortion of competition due to more equal standards for EU & non-EU suppliers	19.51%	10.98%	19.51%	**15.85%**	**24.39%**	9.76%

It should also be noted that stakeholders have indicated various disadvantages which they experience from current lack of regulation in terms of the status quo, which they expect to improve if a general duty is introduced at EU level. These benefits relate to an improvement in competiveness through the levelling of the playing field so that competitors, peers, suppliers and third parties will be subjected to the same standard, as well as increasing leverage with third parties in the value chain through the introduction of a non-negotiable standard. For example, companies have indicated that they are currently struggling to achieve effective results due to having small market shares in certain countries, or buying only a small percentage of the products produced by a specific supplier. If a large number of the other buyers were subject to the same due diligence standards, the effectiveness of their efforts would increase significantly, improving their competiveness and potentially reducing their existing costs. These benefits are difficult to quantify, but should be borne in mind, given that they could be significant, and were raised by business stakeholders as one of the most important reasons for the introduction of a mandatory due diligence requirement.

Innovation

The impacts on innovation are difficult to assess ex ante. As concerns companies' overall innovative capacities, higher costs generally tie up financial resources, which cannot be spent on technological research and development or business model development. As a result, companies that have to comply with tight due diligence regulations might suffer from lower levels of innovation compared to competitors that do not have to comply with these regulations, with adverse implications for companies' medium- to long-term competitiveness.

However, there may also be opposite impacts on companies' innovative capacities. While the impact of new DD policies on new technologies and business processes is limited, new DD regulation might transform companies' value chain management procedures and potentially increase the adoption of cost-efficient tracking and surveillance technologies. Some authors argue that sustainability measures can have an impact on a company's operational efficiency and innovation.[1377] Accordingly, sustainability measures can provide opportunities for innovations as they can lead to the creation of new, more ecological products or new processes and logistics solutions.

Trying to produce more environmental and socially friendly can help to find new solutions and improve existing or invent new products. A consulting report found, for example, examining strategic decisions based on the criterion of sustainability that truly innovative companies have put sustainability at the heart of their business.[1378] It is, furthermore, explained that sustainability-driven innovation is about improving business operations and processes to become more efficient and reduce costs, but it is also about insulating a business from the risk of resource price shocks and shortages, which can all together provide significant economic benefits.[1379] Similarly, other authors studied the sustainability initiatives of 30 large corporations and found that "sustainability is a mother lode of organizational and technological innovations that yield both bottom-line and top-line returns".[1380] The authors argue that companies which aim to meet emerging norms and more stringent future environmental requirements gain time to experiment with materials, technologies, and processes.

- **The impacts of new technology solutions on the costs of due diligence**

Digitalisation and new technology tools hold the potential to provide unprecedented solutions to identify, address and eliminate human rights infringements and environmental challenges. As outlined in the company-level impact assessment, companies of all sizes would face substantial additional costs related to compliance with more comprehensive mandatory DD regulations, particularly full human rights DD throughout companies' value chains. Costs related to the collection of information, e.g. audits conducted either through companies own employees or external services suppliers, are among the highest cost factors for companies.

Emerging tracking and software solutions hold the potential to decrease companies' costs substantially when it comes to accounting for human and environmental rights in company operations and along global value chains. The survey responses indicate that cost savings resulting from new technological advancements have not been taken into consideration by the vast majority of the respondents.

As outlined by the World Business Council for Sustainable Development, "[n]ew technologies [can] enable companies and other stakeholders to receive information that indicates the violation of people's land property, whether products come from verified suppliers, or if health and safety standards are being respected. Satellites, drones, balloons and other aerial vehicles can monitor land, natural ecosystems, movement of materials and products from origin to points of sale. Smart sensors, like radio-frequency identification (RFID) and smart dust are small to microscopic wireless technologies used

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[1377] E.g. Eccles and Serafeim argue that including ESG issues in their sustainability framework leads to cost savings for companies through innovation, resource efficiency, and revenue enhancements due to sustainable products. Eccles, R. G., and Serafeim, G. (2013). The performance frontier: Innovating for a sustainable strategy. Harvard Business Review, May 2013, 50-60. Available at https://hbr.org/2013/05/the-performance-frontier-innovating-for-a-sustainable-strategy.

[1378] Deloitte (2012). Sustainability for consumer business companies. A story of growth. Available at https://www2.deloitte.com/hr/en/pages/consumer-business/articles/sustainability-for-consumer-business-companies.html.

[1379] Capozucca, P. and Sarni, W. (2012). Sustainability 2.0 - Using sustainability to drive business innovation and growth. Available at: https://www2.deloitte.com/us/en/insights/deloitte-review/issue-10/sustainability-2-0-innovation-and-growth-through-sustainability.html

[1380] Nidumolu, R., Prahalad, C.K. and Rangaswami, M.R.(2009). Why Sustainability Is Now the Key Driver of Innovation. Harvard Business Review, September 2019. Available at: https://hbr.org/2009/09/why-sustainability-is-now-the-key-driver-of-innovation.

to tag items with unique identification, gather data on materials, physical environment and natural ecosystems or simply track and trace materials and/or products (often without requiring human intervention on the ground)."[1381]

WBCSD highlights a number of examples for how new technologies can retrieve DD-relevant information from workers, suppliers and other stakeholders. The food products company Unilever, for example, reports to use "technology to get closer to the reality of the situation for workers on the ground or to improve the traceability and transparency of our supply chain."[1382]

For example, the Responsible Labor Initiative (RBA), a multi-industry, multi-stakeholder initiative that is, amongst others, supported by many large multinational companies, uses mobile technology for worker surveys, training and helplines.[1383] According to RBA, it "has been at the forefront of addressing forced labor through the application of advanced due diligence standards, tools and programs in the global supply chains of its members."[1384] At the same time, they stress that "in order to accelerate change, this due diligence must be harmonized across multiple industries that share recruitment supply chains to drive labor market transformation through collective action. To catalyze this, the RBA launched the Responsible Labor Initiative (RLI), a multi-industry, multi-stakeholder initiative focused on ensuring that the rights of workers vulnerable to forced labour in global supply chains are consistently respected and promoted."

Microsoft, a member of RBA, combines a digital platform technology and other processes to build "foundational systems to ensure accountability and efficiencies in Microsoft's programs. Investments in technology solutions such as the Audit Management System, SEA Academy, and customized dash-boards enable strategies, process efficiencies, and insights to meet its sustainability objectives. These solutions empower business decision makers to consume real-time information and make optimal sustainability-related decisions. Interacting with partners through Microsoft's technology platforms also builds cross-team trust and a shared understanding of information.

Similarly, Dell "utilized a mobile training platform as research revealed it can be difficult for suppliers to pull large groups of people off the manufacturing floor for training, yet 80 percent of workers in its suppliers' factories use mobile phones. Because mobile-based training is delivered directly to workers, it is cost-effective for suppliers and easy for Dell to scale globally.[1385]

Tracking technologies for physical goods, such as raw materials, but also intermediate and final products, might become an essential component of DD processes in the future. Without making references to human rights DD obligations, several studies on supply chain management already report a great potential for tracking technologies and "Big Data" analysis in the supply chain and logistics management. Indeed, many industries

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[1381] wbcsd.2018. Is technology a game-changer for human rights in corporate value chains? 27 November 2019. World Business Council for Sustainable Development, Geneva. Available at https://www.wbcsd.org/Overview/Panorama/Articles/Is-technology-a-game-changer-for-human-rights-in-corporate-value-chains.
[1382] Unilever Human Rights Progress Report. 2017. Available at https://www.unilever.com/Images/human-rights-progress-report_tcm244-513973_en.pdf.
[1383] RBA is the world's largest industry coalition dedicated to corporate social responsibility in global supply chains. RBA aims to achieve a global electronics industry that creates sustainable value for workers, the environment and business. Its members, suppliers and stakeholders collaborate to improve working and environmental conditions through leading standards and practices.
[1384] RBA (2019), Promoting the rights of workers vulnerable to forced labor globally, article by Bob Mitchell, accessed at http://www.responsiblebusiness.org/initiatives/rli/
[1385] RBA 2018. RBA Compass Awards 2018. Available at http://www.responsiblebusiness.org/publications/rba-compass-awards-case-studies-2018/.

already show increasing investments in these technologies, e.g. big data and blockchain tools.[1386]

It should be noted that these investments are still generally driven by traditional business demands such as sales, inventory and operations planning and not yet by human rights or environmental DD considerations or policy requirements respectively. Regarding the potential of new tracking technologies, for example, a study commissioned by the European Commission (2015) reports that "numerous drivers are fuelling the growth of advanced tracking systems […]." The authors also stress that "the cost of implementing the systems have shrunk in the last years and have become affordable for most companies. These costs were pushed down by another driver: the harmonisation of standards across the field."[1387]

On current trend, companies still mainly aim to streamline their operations to achieve cost savings along their value chains. Arviem, a technology tracking and software technology provider, for example, reports that supply chain inefficiencies are very costly to businesses, which still rely on "a large amount of point-to-point communication with outdated processes that are heavily dependent on email and phone communication. It involves controlling and monitoring a product's flow from the procurement of raw materials to the distribution of the final product to the end user." They also state that "[d]espite the availability of several technological solutions, many companies still lack end to end visibility to their entire supply chain. This is due to the silos existing between people, processes and technology. This leads to inefficiencies as the supply chain is slowed down by the large and complex network of point-to-point communications."[1388] They published two White Papers on supply chain visibility in the chemical and food products industries, which present supply chain visibility solutions and cargo tracking and monitoring technologies[1389].

For the further development of these solutions with respect to human rights and environmental DD needs, private sector providers may benefit from academic research-based policy guidelines. For the textiles industry, for example, a recent Delphi study, investigated and classified factors influencing traceability implementation and traceability-related information that demands recording and sharing with businesses and customers. Based on expert analyses, the authors conclude, for example, that origin,

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[1386] BCG. 2018. Pairing Blockchain with IoT to Cut Supply Chain Costs. Available at: https://www.dhl.com/content/dam/downloads/g0/about_us/innovation/CSI_Studie_BIG_DATA.pdf; McKinsey 2016. Big data and the supply chain: The big-supply-chain analytics landscape. Available at https://www.mckinsey.com/business-functions/operations/our-insights/big-data-and-the-supply-chain-the-big-supply-chain-analytics-landscape-part-1; European Commission 2015. Traceability across the Value Chain
Advanced tracking systems. Business Innovation Observatory Contract No 190/PP/ENT/CIP/12/C/N03C01. Available at https://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=2&ved=2ahUKEwjJyf7esIfkAhUBaFAKHY5wChMQFjABegQIABAC&url=https%3A%2F%2Fec.europa.eu%2Fdocsroom%2Fdocuments%2F13393%2Fattachments%2F2%2Ftranslations%2Fen%2Frenditions%2Fnative&usg=AOvVaw2PXz_OJiA0-B4C2xmTbuKj; DHL 2013. Big Data in Logistics. Available at https://www.dhl.com/content/dam/downloads/g0/about_us/innovation/CSI_Studie_BIG_DATA.pdf; BVL International (2013). Trends and Strategies in Logistics and Supply Chain Management.

[1387] European Commission 2015. European Commission 2015. Traceability across the Value Chain
Advanced tracking systems. Business Innovation Observatory Contract No 190/PP/ENT/CIP/12/C/N03C01. Available at https://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=2&ved=2ahUKEwjJyf7esIfkAhUBaFAKHY5wChMQFjABegQIABAC&url=https%3A%2F%2Fec.europa.eu%2Fdocsroom%2Fdocuments%2F13393%2Fattachments%2F2%2Ftranslations%2Fen%2Frenditions%2Fnative&usg=AOvVaw2PXz_OJiA0-B4C2xmTbuKj.

[1388] Arviem. 2018. How IoT and Big data are accelerating the supply chain industry?. Available at https://arviem.com/de/iot-and-big-data-supply-chain-industry/.

[1389] Arviem. 2018. White papers on "Chemical Supply Chain Visibility" and "Food Supply Chain Traceability". Available at https://arviem.com/white-papers/.

composition, manufacturer/supplier details, product specifications, and composition can create decisive knowledge of traceability for the textile and clothing supply chain.[1390]

New legal obligations regarding human rights and environmental DD would add another dimension to value chain management on top of already existing "cost drivers", which are currently the key determinants driving companies' to adopt and expand supply chain management technologies. Even though it is difficult to project which companies and how many of them invest and adopt new technologies in the future, including technologies that allow them to extract critical DD-relevant information, we expect a significant rise in the utilisation of these technologies. While large businesses seem to be the global frontrunners, these technologies could, in principle, be applied by SMEs and micro businesses. Platform-based solutions, which might be operated by a small number of large providers (like Amazon for online intermediation and data cloud services), could become a low-cost and therefore affordable option for SMEs.

It is difficult to project the time horizon until a more rapid, cross-industry adoption will take place. New EU regulations, including specific policy guidelines on required metrics and/or EU-driven standardisation initiatives could spur innovation in new technologies, software solutions, cross-industry platforms and platform-based business models. The latter could comprise companies that offer audit-based data collections, data management, hazard recognition and early-warning systems, but also companies that provide primary data on the basis of on-site audits. A greater adoption of technology-based services, internally and externally-sourced, is likely to translate to significant cost savings across DD activities. However, a more detailed assessment of the technological possibilities, opportunities and pecuniary impacts of new technologies on human rights and environmental DD would require a separate study as it is beyond the scope of this analysis.

3.1.3 Company-level Benefits

In this section, we discuss potential company-level benefits that are likely to result from additional voluntary and mandatory due diligence (DD) activities.

The following assessment is based on a literature review as well as on the survey results from the business survey. In the absence of quantitative studies, the assessment will mainly discuss qualitative aspects. The lack of quantitative studies is due to the fact that it is extremely difficult to isolate the effects of one responsible business conduct measure from another since these tend to create multiple intermediate effects that play into each other.[1391] In addition, it has to be noted that most existing studies assess benefits arising from general concepts such as sustainability reporting or corporate social responsibility (CSR) activities and do not assess benefits accruing from due diligence activities in particular. Similarly, most studies assess business practices rather than impacts from regulations and laws which may not have identical impacts. This has to be kept in mind when reading the following assessment.

[1390] Agrwal, T. K. and Rudrajeet, P. 2019. Traceability in Textile and Clothing Supply Chains: Classifying Implementation Factors and Information Sets via Delphi Study. Sustainability 2019, 11(6), 1698. Available at https://www.mdpi.com/2071-1050/11/6/1698/htm.

[1391] OECD (2016). Quantifying the Costs, Benefits and Risks of Due Diligence for Responsible Business Conduct Framework and Assessment Tool for Companies- June 2016. Available at https://mneguidelines.oecd.org/Quantifying-the-Cost-Benefits-Risks-of-Due-Diligence-for-RBC.pdf

Other EU Impact Assessments of legislation with similar elements assess economic benefits in very different areas and tend to remain relatively broadly. The main conclusions which are relevant for this impact assessment are summarised in the following paragraphs, for a more comprehensive and detailed description see the literature review section.

The Impact Assessment on the EU Non-financial Reporting Directive (EUNFRD) concludes that the regulation is expected to provide benefits for companies at an internal and external level. Internally, companies are expected to benefit from better employee relations, improved management systems and internal processes. Externally, companies are expected to benefit from an enhanced reputation, better perception by and dialogue with stakeholders, as well as easier access to capital. The impact assessment also expects overall economic benefits from better risk management and allocation of capital, enhanced trust in business and better resource management. Similarly, the Impact Assessment on the EU Conflict Minerals Regulation indicates that the main benefits for companies are expected from reputational effects.

The Impact Assessment on a proposed EU Regulation on Sustainable Investment (2018) focuses on general economic impacts rather than firm-specific impacts and concludes that the regulation could provide economic benefits by fostering competition, efficiency, innovation and the overall competitiveness of the European sustainable finance market.

The Impact Assessment of the EU Environmental Crime Directive (ECD) (Directive 2008/99/EC), also expects economic benefits in terms of a more balanced competition within the European market and improved competitiveness of European products internationally due to an improved confidence of third countries businesses in the quality of products from the EU.

The Impact Assessment of the Seveso III Directive discusses mainly costs for operators, but also expects some benefits related to improved risk management (the risk of major accidents is reduced and the costs of major accidents are avoided). As a result of a better safety management system business performance and competitiveness are expected to improve, which increase efficiency and processes.

Some of the benefits which were pointed out to during the interviews related to increased legal certainty, creation of a level playing field and benefits from EU-wide harmonization.

Regarding legal certainty it was argued that a due diligence regulation will help companies to respond to those risks that are considered to be of highest priority or most severe, rather than focusing on those which are or may be most exposed in the public domain and therefore criticized (see section 4.4. Due diligence practices in own operations). Especially when budgets are limited, clear legal requirements could help to prioritize and focus on the most important areas. This would enable them to cover their reputational risks by complying with a clear law.

Another benefit of a new due diligence regulation which was mentioned during the interviews is that it would create a level-playing field for companies in the EU since all companies would have to comply with the same requirements (see section 5.4. Option 4: Regulation requiring mandatory due diligence as a standard of care).[1392]

In the survey it was also argued that harmonisation of due diligence requirements at the EU level would reduce the complexity, uncertainty as well as the cost of ensuring and demonstrating compliance with different laws and requirements (see section 6.1. Harmonisation). In addition, it was argued that standardization amongst European companies and brands could increase efficiency and improve coordination with business partners since all would be speaking the same "language" and be liable to the same requirements.

Finally, it was pointed out that a new regulation on due diligence would assumedly increase the effectiveness of due diligence activities of companies which are already following a voluntary due diligence policy. This would not only increase the motivation of companies and their staff who are already frontrunners, but it would also increase the impacts of the due diligence measures in third countries and could therefore potentially reduce the costs for the individual company for their due diligence activities.[1393]

The literature review of academic studies and business reports (for more details, see section 1) found that economic benefits from due diligence activities can arise in different areas. The main economic benefits are described in four main areas.

1. brand and image reputation,
2. human resources,
3. risk management, operational efficiency and innovation,
4. and financial and stock performance, as well as cost of capital.

The first area of benefits is a company's brand image and reputation. A company's CSR and sustainability activities can improve its brand image and reputation, which can turn into concrete economic benefits in the form of higher sales and the ability to charge higher prices than competitors which do not engage in sustainability measures. For example, a regular online survey among 30,000 consumers, revealed that most consumers (55%) were willing to pay extra for products and services from companies that are committed to positive social and environmental impact. [1394] Another study found that consumers perceived greater benefit and value in the product of a socially responsible company and were willing to pay 10% more for such products. [1395] However, it was also pointed out that (see section 4.12 Incentives for undertaking due diligence in the Market Practices chapter) reputational effects mainly work for companies which are consume-faced and they are less of a benefit for companies who are intermediaries, work in public procurement or in the public sector. [1396]

The second type of economic benefits can arise in the area of human resources. CSR and sustainability activities can increase the attractiveness of a company for employers and help to attract or retain high qualified staff and increase the loyalty and motivation of

[1392] It was also argued that companies which are already frontrunners would not be impacted by a new legislation because they are most likely already fulfilling the requirements (see section 5.4.3. On due diligence as a defence).
[1393] Some companies argued in the interviews (see section 4.8. Leverage and the ability of individual companies) that the "inaction of other [companies] hampers the effectiveness of [a company's] due diligence efforts", i.e. that their own efforts would be more effective if other companies which are currently not pursuing due diligence measures would also do so.
[1394] Nielsen (2014). Doing Well By Doing Good. Available at https://www.nielsen.com/us/en/insights/reports/2014/doing-well-by-doing-good.html
[1395] Ferreira, D. A. and Avila,M.G. and Dias de Faria, M. (2010). Corporate social responsibility and consumers' perception of price. Social Responsibility Journal, Vol. 6 Issue: 2, pp.208-221. Available at https://doi.org/10.1108/17471111011051720
[1396] It is argued that if the company name is not relevant for the public and consumers do not know a company, there is no risk of public pressure.

employees, leading to higher efficiency and productivity. For example, an often-quoted experimental study concludes that company's corporate social performance can lead to a competitive advantage by attracting and retaining high-quality candidates. [1397]

The third area where economic benefits can arise comprises improved risk management, operational efficiency and innovation. As international supple chains include many different suppliers and stakeholders in different regions, due diligence can foster a comprehensive risk management process to identify, assess, prevent and mitigate the risks within these complex supply chains. This reduced risk can result in a concrete economic impact. For example, an academic study assessing the impact of corporate social performance on market-based company risk in Europe finds that better corporate social performance – especially in the social dimension – can increase company value through lower company risk. [1398] It was also pointed out in the interviews that a lack of undertaking due diligence is a greater financial risk to the company than doing due diligence (see section 5.4. Option 4: Regulation requiring mandatory due diligence as a standard of care).

At the same time some authors argue that sustainability measures can have an impact on a company's operational efficiency and innovation. Accordingly, sustainability measures can lead to a more efficient use of resources and therefore result in cost-savings for a company. These sustainability and resource efficiency measures can then provide opportunities for innovations, e.g. in the form of new products, process or new logistic solutions (please see also section 3.1.2 Company-level Costs for a discussion of impacts on innovation). A large meta-analysis concluded that most assessed studies show a positive relationship between sustainability and operational performance. [1399] The authors of the analysis therefore argue that good corporate environmental practices positively influence the competitiveness of companies and lead to better corporate performance. A consulting report on sustainability for consumer business companies also concludes that sustainability is recognised increasingly as a primary driver for strategic product and business model innovation. [1400]

The fourth area in which sustainability measures can produce economic benefits are a company's financial and stock performance as well as capital costs. These are both possible economic benefits that could result from different due diligence activities or measures taken by companies, which increase a company's reputation and therefore foster its sales. This, in turn, leads to higher revenues or better stock market performance which then also allow a company to get capital at lower cost. Companies with good sustainability records may also be more attractive to investors due to the expectation of lower risks and reduced information asymmetries from disclosure standards. A recent meta-analysis of about 2,200 individual studies finds that the business case for environmental, social, and governance (ESG) investing is empirically very well founded. [1401] Another meta-analysis concludes that 80% of the assessed

[1397] Greening, D. W., and Turban, D. B. (2000). Corporate Social Performance as a Competitive Advantage in Attracting a Quality Workforce. *Business & Society*, *39*(3), 254–280. https://doi.org/10.1177/000765030003900302.
[1398] Sassen, R.; Hinze, A.K.; Hardeck, I. (2016). Impact of ESG factors on firm risk in Europe. Journal of Business Economics, Volume 86, Issue 8, pp 867–904. Available at https://link.springer.com/article/10.1007%2Fs11573-016-0819-3
[1399] Clark, Gordon L. and Feiner, Andreas and Viehs, Michael (2015). From the Stockholder to the Stakeholder: How Sustainability Can Drive Financial Outperformance. Available at SSRN: https://ssrn.com/abstract=2508281 or http://dx.doi.org/10.2139/ssrn.2508281 NOTE 40
[1400] Deloitte (2012). Sustainability for consumer business companies. A story of growth. Available at https://www2.deloitte.com/hr/en/pages/consumer-business/articles/sustainability-for-consumer-business-companies.html
[1401] Bassen, A. and Busch, T. and Friede, G. (2015). ESG and financial performance: aggregated evidence from more than 2000 empirical studies, Journal of Sustainable Finance & Investment, 5:4, 210-233, DOI: 10.1080/20430795.2015.1118917

studies find that a company's stock price performance is positively influenced by its good sustainability practices.[1402]

Some of these different types of benefits can be linked more directly to concrete due diligence measures and may be experienced also in the short run, while other benefits are more indirect results from sustainability activities and may be experienced rather in the long-term.

In order to better understand how different impacts from due diligence activities are interlinked and how they ultimately affect a company's costs or revenues and translate into concrete economic benefits, the OECD has groupeddifferent potential benefits from due diligence measures into intermediate benefits and final impacts (Figure 8.7). The intermediate benefits are the more immediate or direct benefits resulting from the due diligence activities. In the longer term, these translate into concrete financial benefits by either reducing a company's cost or enhancing the revenue.

When comparing a company's costs and benefits from due diligence activities it is therefore important to not only consider impacts which may be felt more immediately and can be linked more directly to due diligence measures, such as an improved brand image and reputation, improved governance, transparency and management of supply chains, leading also to reduced operational and strategic company risks. It is also important to take into account how due diligence activities can turn into concrete financial benefits in a longer term, although these may be linked less directly to the due diligence activities since they are influenced also by other factors. The OECD report, for example, foresees that an improved operational knowledge, i.e. a deeper knowledge of a company's supply chains, resulting reduced operational and strategic risks and improved process and product innovations, will have a cost reducing effect by increasing a company's efficiency and reducing risks, while at the same time it will create more growth opportunities and thereby increase a company's revenue. Another channel how due diligence activities can reduce a company's costs in the longer term and enhance revenues is through its improved reputation. According to the report, a better reputation improves a company's license to operate, its customer perception, brand loyalty and ability to charge a price premium. In addition, the improved reputation can open up sources of funding which were previously not available. These intermediate benefits are expected to then translate into a reduction of capital costs, improve a company's position in the market, increase its brand equity and create more growth opportunities.

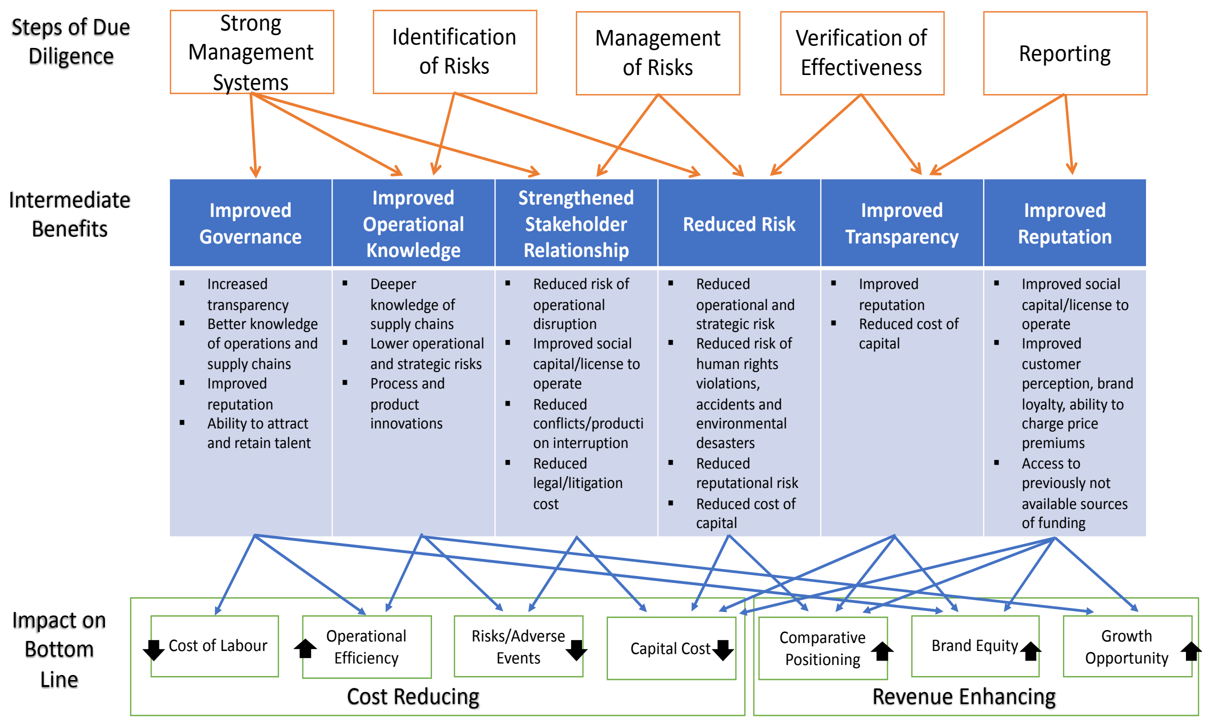
The following assessment of the different policy options and the possible economic benefits for firms will be based on the literature review of the described four main areas of economic benefits as well as on the results from the business surveys. As the concrete design of a possible new regulations is yet to be developed, expected economic benefits can only be described in general and any assumptions about possible economic benefits depend largely on the content and design of a future regulation.

Again, these reputational impacts discuss the potential benefits which companies could gain in relation to the status quo. However, stakeholders have expressed a discontent with the existing legal landscape for reasons relating to reputational risks that they are currently experiencing. Notably, companies indicated that their top incentive to

[1402] Clark, Gordon L. and Feiner, Andreas and Viehs, Michael (2015). From the Stockholder to the Stakeholder: How Sustainability Can Drive Financial Outperformance. Available at SSRN: https://ssrn.com/abstract=2508281 or http://dx.doi.org/10.2139/ssrn.2508281 undertake due diligence is, or has been, reputational risks. The growing number of investors-driven due diligence requirements are sharply bringing into focus the reputation of the investee in undertaking effective due diligence. Case law and interviewees both reflect the perception that companies with a good reputation may in fact be legally targeted on the basis of their public commitments.

It is expected that these existing and significant reputational risks may be reduced through the introduction of a general due diligence duty. It is not possible to quantify these benefits at this early stage. However, given the significance which business stakeholders place on reputational risks, it is likely that the most significant reputational benefits from a mandatory due diligence requirement may result from a *reduction in existing reputational risks* rather than an enhancement of existing reputational benefits.

Figure 8.7: Impact Chain for Benefits from Due Diligence Activities[1403]



- **Option 1: No policy change**

As for all other impact areas, the possible economic benefits for firms and possibly industries depend on the development of the policies in EU Member States and the extent to which companies take due diligence measures on a voluntary or individual basis. As described in the Regulatory Options section, it is expected that due diligence requirements will increasingly be introduced by EU Member States, however it is unclear what obligations these will entail for companies and whether individual companies might take voluntary initiatives. Economic benefits for companies or specific sectors are therefore difficult to assess.

<u>Expected company benefits resulting from current DD activities</u>

[1403] Ibid.

When companies were asked about the most significant benefits for their company resulting from their current due diligence activities[1404] (for human rights and environmental impacts through the supply chain), the greatest benefits were seen in greater supply chain certainty (42%), lower operational risks (34%) and greater legal certainty (33%). In these three areas of benefits respondents saw either significant or very significant benefits for their company rather than moderate, some or no benefits. The results suggest that these three benefits are the perceived main benefits for companies from their voluntary due diligence activities since the question addressed benefits from current activities which are currently taken without an EU-wide regulation that requires firms to take due diligences measures. No benefits from the current activities were seen mainly for lower costs of capital (27%) and greater leverage over non-EU suppliers (21%). It has to be acknowledged though that only one third of the responding companies answered this question at all.

Table 8.41: Expected additional benefits from current DD activities

	No benefits	Some benefits	Moderate benefits	Significant benefits	Very significant benefits	Do not know
Reputation-based increases in revenue (through consumption/brand value)	16.19%	21.90%	28.57%	12.38%	10.48%	10.48%
Reputation-based increases in investment	16.50%	20.39%	25.24%	17.48%	6.80%	13.59%
Improved quality / life-cycle of products / services	19.80%	20.79%	22.77%	18.81%	3.96%	13.86%
Greater supply chain certainty	11.65%	21.36%	18.45%	25.24%	16.50%	6.80%
Greater legal certainty	14.85%	18.81%	23.76%	22.77%	9.90%	9.90%
Greater leverage over non-EU supplier provided by non-negotiable standard	21.15%	22.12%	20.19%	19.23%	2.88%	14.42%
Lower operational risk	12.50%	20.19%	25.96%	26.92%	6.73%	7.69%

[1404] Q21 in the Business Survey. For the full survey results, please see the Annex.

Lower cost of capital (due to lower risk)	27.00%	23.00%	19.00%	11.00%	1.00%	19.00%
Reputation-based increases in revenue (through consumption/brand value)	16.19%	21.90%	28.57%	12.38%	10.48%	10.48%
Reputation-based increases in investment	16.50%	20.39%	25.24%	17.48%	6.80%	13.59%
Q21 Business Survey; 106 responses.						

In regard to possible benefits for companies' brand image and reputation these depend largely on the activities taken by companies either due to a national law to which they are subject or due to voluntary initiatives. Those companies which are frontrunners and advance due diligence activities on their own behalf and succeed to communicate well about these activities can also experience benefits in terms of an improved brand image and reputation which may result in higher sales of their products. At the same time, the relative impact of enhanced reputation on a companies' total sales may not generate returns sufficient to cover the additional cost for compliance with legal standards.

For this option there are no specific economic benefits expected for firms arising from an increased ability to attract and retain employees. This depends, however, as discussed on how due diligence requirements develop in EU member states. Companies which improve their due diligence policies and activities as a result of a national legislation or voluntarily, could in theory experience economic benefits if they can attract better qualified employees and these are better motivated.

If companies would advance their due diligence on their own initiatives or national laws in EU Member States would require companies to take due diligence measures, it could be expected that economic benefits for companies arising from better risk management, operational efficiency and innovation could arise. These are also the areas where most benefits are expected by business respondents (greater supply chain certainty (42%) and lower operational risks (34%)). However, this is difficult to predict.

Economic benefits in the form of better financial and stock performance under this option would be possible for those companies which improve their due diligence, either as part of national regulations or voluntarily. Whether any economic benefits can be expected would therefore depend on the individual actions taken by firms, which are difficult to predict.

- **Option 2: New voluntary guidelines / guidance**

Additional benefits arising from new EU guidelines are expected in similar areas as the observed benefits from ongoing activities under option 1.[1405] Respondents mainly expect significant or very significant additional benefits from new guidelines for their supply chain certainty (22%), for a greater leverage over non-EU supplier provided by non-negotiable standards (20%) or lower operational risks (16%). However, there is also some ambiguity in the responses since also 30% and 27% of respondents answered that they did not expect any additional benefits for their company for greater leverage over non-EU supplier provided by non-negotiable standard and lower operational risks. In addition, 33% and 30% do not expect any additional benefits in the form of lower cost of capital (due to lower risks) or benefits stemming from the elimination of a comparative disadvantage between companies regulated by different EU Member States.

Table 8.42: Expected additional benefits from Option 2

	No benefits	Some benefits	Moderate benefits	Significant benefits	Very significant benefits	Do not know
Reputation-based increases in revenue (through consumption/brand value)	23.40%	20.21%	20.21%	11.70%	4.26%	20.21%
Reputation-based increases in investment	24.47%	22.34%	18.09%	9.57%	5.32%	20.21%
Improved quality / life-cycle of products / services	28.72%	15.96%	21.28%	9.57%	3.19%	21.28%
Greater supply chain certainty	20.65%	15.22%	26.09%	17.39%	4.35%	16.30%
Greater legal certainty	26.67%	17.78%	21.11%	7.78%	7.78%	18.89%
Greater leverage over non-EU supplier provided by non-negotiable standard	29.67%	15.38%	16.48%	14.29%	5.49%	18.68%
Lower operational risk	27.17%	15.22%	27.17%	10.87%	5.43%	14.13%
Lower cost of	32.61%	17.39%	21.74%	5.43%	4.35%	18.48%

[1405] Q24 in the Business Survey. For the full survey results, please see the Annex.

capital (due to lower risks)						
Less distortion of competition due to more equal standards for EU & non-EU suppliers	28.26%	14.13%	20.65%	13.04%	6.52%	17.39%
No comparative disadvantage between companies regulated by different EU Member States	30.11%	12.90%	19.35%	10.75%	7.53%	19.35%
Q24 Business Survey; 97 responses.						

Possible benefits for firms are similar to those under option 1, i.e. they will depend primarily on individual companies' actions taken to follow national laws or for strategic purposes as voluntary initiatives. New guidance on due diligence provided by the EU may facilitate companies taking due diligence actions and benefiting from enhanced reputation. However, the impact is expected to be negligible since already a large amount of guidance exists which can be followed by companies interested in pursuing due diligence activities.

Similar to option 1, possible economic benefits in the area of human resources depend on voluntary due diligence actions taken by individual companies since a new guidance does not prescribe companies to take any activities. As a large amount of guidance exists already, it is not expected that economic benefits may arise for companies in regard to their human resources.

Similarly, it is not expected that new voluntary guidance will provide an incentive for companies to introduce or improve existing due diligence policies to an extent which would provide tangible economic benefits from better risk management, operational efficiency or innovation.

Economic benefits in the form of better financial performance of lower cost of capital are not expected to be significant when introducing new voluntary guidance. In order to experience tangible economic benefits such as better stock performance or lower cost of capital a company needs to take substantial action which has to be communicated and noted by the stock and capital markets. It is expected that the provision of new guidance is not able to facilitate these changes and resulting benefits.

- **Option 3: New regulation requiring due diligence reporting**

Business respondents to the survey expect mostly the same additional benefits from a new regulation requiring due diligence reporting as under option 2 only that shares of respondents which expect significant or very significant benefits increase.[1406]

[1406] Q33 in the Business Survey. For the full survey results, please see the Annex.

Respondents mainly expect benefits in the form of greater supply chain certainty (32%), greater legal certainty (29%), greater leverage over non-EU suppliers provided by a non-negotiable standard (24%), and lower operational risks (22%). However, a similar share of the respondents expects no benefits for lower operational risks (32%) and lower cost of capital (34%) indicating some ambiguity in the responses which may also be due to the lack of details that could be provided about the design of the surveyed regulatory options.

Table 8.43: Expected additional benefits from Option 3

	No benefits	Some benefits	Moderate benefits	Significant benefits	Very significant benefits	Do not know
Reputation-based increases in revenue (through consumption/brand value)	30.23%	12.79%	27.91%	9.30%	6.98%	12.79%
Reputation-based increases in investment	30.23%	15.12%	23.26%	12.79%	4.65%	13.95%
Improved quality / life-cycle of products / services	33.72%	15.12%	19.77%	9.30%	5.81%	16.28%
Greater supply chain certainty	25.88%	18.82%	14.12%	23.53%	8.24%	9.41%
Greater legal certainty	24.71%	15.29%	17.65%	17.65%	11.76%	12.94%
Greater leverage over non-EU supplier provided by non-negotiable standard	27.06%	14.12%	21.18%	17.65%	5.88%	14.12%
Lower operational risk	31.76%	16.47%	20.00%	15.29%	7.06%	9.41%
Lower cost of capital (due to lower risks)	34.12%	18.82%	15.29%	10.59%	2.35%	18.82%
Less distortion of competition due to more equal standards for EU & non-EU suppliers	27.91%	11.63%	23.26%	18.60%	5.81%	12.79%

No comparative disadvantage between companies regulated by different EU Member States	25.84%	13.48%	17.98%	17.98%	5.62%	19.10%
Q33 Business Survey; 89 responses.						

The potential economic benefits for firms resulting from mandatory due diligence reporting, depend on the extent to which mandatory reporting requirements enact changes in companies' policies. If public reporting leads to a revision of company policies and improvements of their due diligence activities throughout their supply chains, this could lead to economic benefits for companies in the EU, especially for those which are considered as frontrunners. Since reporting will be mandatory there is an automatic channel of communicating good due diligence policies to the broader public which in turn can promote a company's brand image and reputation. This is in turn the prerequisite for a company to benefit from increased sales and revenues and benefit from concrete financial compensation.

Also, other EU Impact Assessments of regulations with reporting requirements expect reputational benefits for companies. The Impact Assessment on the EU Non-Financial Reporting Directive concludes that the regulation is expected to provide benefits for companies at an internal and external level. Externally, companies are expected to benefit from an enhanced reputation, better perception by and dialogue with stakeholders.

Similarly, the EU impact assessment on the Conflict Minerals Regulation indicates that the main benefits for companies are expected from "unquantifiable externalities which can be used for marketing purposes such as public image, Corporate Social Responsibility (CSR) and consumer satisfaction".[1407]

Similar to the discussion of potential benefits from brand image and reputation, the economic benefits related to better human resources depend on the extent to which a mandatory reporting requirement leads to changes in companies' due diligence activities. If a reporting requirement leads to due diligence activities which increase a company's reputation, then there can also be economic benefits from the possibility to attract better staff and have lower turnover rates. The Impact Assessment on the EU Non-Financial Reporting Directive also expects internal benefits for companies relating to their human resources as companies are expected to benefit from better employee relations.

Similar to the discussion of potential benefits from brand image and reputation and that related to human resources, economic benefits arising from better risk management, operational efficiency and innovation will depend on the extent to which mandatory reporting requirement are able to enact changes in company's due diligence policies and behaviour. The impact assessment of the EU Non-Financial Reporting Directive stipulates

[1407] See European Commission (2014), Impact Assessment Accompanying the document Proposal for a Regulation of the European Parliament and of the Council setting up a Union system for supply chain due diligence self-certification of responsible importers of tin, tantalum and tungsten, their ores, and gold originating in conflict-affected and high-risk areas. PART 1 (Impact Assessment). Full external report available at https://publications.europa.eu/en/publication-detail/-/publication/dced6d04-92fb-4a20-a499-4dad9974aee7 01aa75ed71a1.0001.01/DOC_3&format=PDF.

expected overall economic benefits from better management of risks and allocation of capital, enhanced trust in business and better resources management.

Again, the potential economic benefits in the form of better financial performance and lower capital cost depend largely on the question of how much change mere reporting requirements can enact changes in behaviour and whether these changes are communicated by the company to its investors and capital markets. Concerning lower capital costs 34% of the survey respondents do not expect any benefits from this regulatory option. In contrast, however, the Impact Assessment of the EU Non-Financial Reporting Directive concludes that the regulation is expected to provide benefits for companies at the internal and external level and external level, of which the latter includes easier access to capital.

- **Option 4: New regulation requiring mandatory due diligence as a legal duty of care**

Survey respondents mainly expect benefits in the form of greater leverage over non-EU suppliers provided by a non-negotiable standard and greater legal certainty (46% each), followed by greater supply chain certainty (44%) and lower operational risks (35%). If no benefits are expected from mandatory due diligence, these are mainly for lower cost of capital (due to lower risks) and reputation-based increases in investment (26% of respondents rated these benefits).[1408]

Table 8.44: Expected additional benefits from Option 4

	No benefits	Some benefits	Moderate benefits	Significant benefits	Very significant benefits	Do not know
Reputation-based increases in revenue (through consumption/brand value)	23.46%	22.22%	14.81%	11.11%	14.81%	13.58%
Reputation-based increases in investment	25.93%	19.75%	18.52%	11.11%	11.11%	13.58%
Improved quality / life-cycle of products / services	24.69%	16.05%	16.05%	14.81%	12.35%	16.05%
Greater supply chain certainty	14.81%	16.05%	18.52%	22.22%	22.22%	6.17%
Greater legal certainty	14.81%	16.05%	16.05%	18.52%	27.16%	7.41%

[1408] Q42 in the Business Survey. For the full survey results, please see the Annex.

Greater leverage over non-EU supplier provided by non-negotiable standard	18.75%	11.25%	13.75%	20.00%	26.25%	10.00%
Lower operational risk	18.52%	16.05%	22.22%	17.28%	17.28%	8.64%
Lower cost of capital (due to lower risks)	26.25%	15.00%	16.25%	12.50%	10.00%	20.00%
Less distortion of competition due to more equal standards for EU & non-EU suppliers	19.51%	10.98%	19.51%	15.85%	24.39%	9.76%
No comparative disadvantage between companies regulated by different EU Member States	17.65%	14.12%	16.47%	15.29%	22.35%	14.12%
Q42 Business Survey; 85 responses.						

Similar to option 3, the potential economic benefits for companies from a new regulation requiring mandatory due diligence depend on the extent to which such due diligence activities are implemented and the extent to which companies succeed in communicating the benefits to their consumers. If a company, as a result of a new EU regulation, implements due diligence activities which are known by consumers, this can contribute considerably to the company's brand image and reputation. Research has shown that this can foster the sales of its products and allow it to charge higher prices. Several studies have found that socially and environmentally responsible companies are able to charge higher prices for their products or experience higher sales rates[1409]. Other researchers even found that consumers were willing to pay 10% more for products from socially responsible companies. This option could therefore provide significant economic benefits for firms related to their reputation and sales. [1410,1411]

In addition, mandatory due diligence requirements would decrease reputational risks. At the moment there is no existing law which reflects and is aligned with public expectations about company behaviour. As a result, a company's reputation can be harmed even if the company is legally compliant. However, if there would be a new due

[1409] Nielsen (2014). Doing Well By Doing Good. Available at https://www.nielsen.com/us/en/insights/reports/2014/doing-well-by-doing-good.html.
[1410] Hainmueller, J. and Hiscox, M. (2015). Buying Green? Field Experimental Tests of Consumer Support for Environmentalism. Working Paper. Available at https://scholar.harvard.edu/hiscox/publications/buying-green-field-experimental-tests-consumer-support-environmentalism.
[1411] Ferreira, D. A. and Avila,M.G. and Dias de Faria, M. (2010). Corporate social responsibility and consumers' perception of price. Social Responsibility Journal, Vol. 6 Issue: 2, pp.208-221. Available at https://doi.org/10.1108/17471111011051720.

diligence law which is more in line with consumers expectations, the company can ensure that it does not suffer reputational harm by complying with the law, i.e. the law would reduce reputational risks for a compliant company and at the same time provide legal certainty. Companies are currently suffering reputational harm when they are accused of unsustainable business practices which are actually legal, but claiming that these practices are legal does not reduce the reputational damage as there is currently such a big gap between what is legal and what is expected by consumers.

However, it may also play a role to which and how many companies the new regulation applies. The more companies it would apply to, the smaller could be the potential economic gains from an enhanced brand image and reputation, at least vis-à-vis other European companies. The reason is that an individual company could not have a competitive advantage from its due diligence activities if all other European companies are taking the same or similar measures. Consumers could then only favour the company's products and be willing to pay higher prices if the company's due diligence policy and measures go beyond those of its European competitors. Vis-à-vis non-European competitors, however, European companies could still benefit from reputational effects. In addition, there could be a first mover advantage for European companies in the global market since the latter is increasingly sensitive to sustainability aspects (investors as well as consumers). The Impact Assessment of the EU Environmental Crime Directive (ECD) (Directive 2008/99/EC), also expects economic benefits from an improved competitiveness of European products internationally due to an improved confidence of third countries businesses in the quality of products from the EU.

Similar to the positive impacts on reputation and brand image, it can be expected that increased due diligence activities by companies will increase their attractiveness for employees. As a result, it can be expected that European companies may be able to attract staff with better qualifications and be more likely to retain good staff.

Different studies have shown that sustainability measures and CSR activities can make a company more attractive for job applicants in the sense that they prefer to work for that company rather than for another company which is perceived less sustainable and/or that a company can compensate with its reputation for less competitive salary packages. One study found that 67% of participants to an online survey preferred to work for a socially responsible company. [1412] And in order to work for a socially responsible company 30-45% of university students would accept a 15% pay cut.[1413]

However, similar to the description of reputation and brand image impacts, benefits related to human resources can also depend on a company's relative advantage and the coverage of companies. If all companies would conduct due diligence measures to a similar extent and would therefore be similarly attractive for employees, a company may be able to benefit less substantially from its due diligence activities. As stated above, vis-à-vis non-European competitors, European companies could still benefit from reputational effects and a potential first mover advantage in the global market.

[1412] Nielsen (2014). Doing Well By Doing Good. Available at https://www.nielsen.com/us/en/insights/reports/2014/doing-well-by-doing-good.html.
[1413] Szeltner, M. and Zukin, C. (2012). Talent Report: What Workers Want in 2012. Study by Net Impact and Rutgers University. Available at https://www.netimpact.org/research-and-publications/talent-report-what-workers-want-in-2012.

If a new EU regulation requires mandatory due diligence, it can be expected that economic benefits for companies arise from better risk management, operational efficiency and innovation. On the one hand, this is an expectation that is underlined strongly by the survey results: greater supply chain certainty (44%) and lower operational risks (35%) were two of the three main benefits expected by respondents from this regulatory option. On the other hand, academic research finds that sustainability measures by firms have a positive impact on the company risk and operational efficiency which translates into concrete economic value. One study[1414] finds that better corporate social performance can decrease a company's risk and thereby increase its value. Another large meta-analysis concludes that 88% of the assessed studies showed that solid environmental, social and governance (ESG) practices result in better operational performance of firms, i.e. that there is a positive relationship between sustainability and operational performance.[1415] Other academic authors found that the inclusion of ESG issues leads to cost savings for firms through innovation and resource efficiency.[1416]

Other EU Impact Assessments also expect economic benefits for competitiveness, efficiency and innovation from new regulations with sustainability requirements for companies. The Impact Assessment on a proposed EU Regulation on Sustainable Investment concludes that the regulation could provide economic benefits by fostering competition, efficiency, innovation and the overall competitiveness of the European sustainable finance market. Similarly, the Impact Assessment of the Seveso III Directive expects benefits related to improved risk management (the risk of major accidents is reduced and the costs of major accidents are avoided). As a result of a better safety management system business performance and competitiveness are expected to improve, which increase efficiency and processes.

It can also be expected that economic benefits for companies arise in the form of better financial or stock performance and access to lower cost of capital if a new EU regulation requires mandatory due diligence and leads to improved due diligence measures taken by companies.

A large body of literature assessed the links between companies' sustainability measures and their financial performance. Empirical evidence of companies' sustainability activities and financial or stock performance largely indicates a positive relationship, although there are also studies which cannot find a direct impact. For example, Clark et al.'s large meta-analysis cited above shows that 80% of the assessed studies find a positive influence of good sustainability practices on stock price performance. Similarly, another empirical study finds that companies which have been employing environmental and social policies over the past perform better regarding stock market and accounting performance.[1417] It finds that stocks of high-sustainability companies outperform those of low-sustainability companies by 4.5% annually.

[1414] Sassen, R.; Hinze, A.K.; Hardeck, I. (2016). Impact of ESG factors on firm risk in Europe. Journal of Business Economics, Volume 86, Issue 8, pp 867–904. Available at https://link.springer.com/article/10.1007%2Fs11573-016-0819-3.
[1415] Clark, Gordon L. and Feiner, Andreas and Viehs, Michael (2015). From the Stockholder to the Stakeholder: How Sustainability Can Drive Financial Outperformance. Available at SSRN: https://ssrn.com/abstract=2508281 or http://dx.doi.org/10.2139/ssrn.2508281.
[1416] Eccles, R. G., and Serafeim, G. (2013). The performance frontier: Innovating for a sustainable strategy. Harvard Business Review, May 2013, 50-60. Available at https://hbr.org/2013/05/the-performance-frontier-innovating-for-a-sustainable-strategy.
[1417] Eccles, R. G., and Ioannou, I. and Serafeim, G. (2014). "The Impact of Corporate Sustainability on Organizational Processes and Performance," Management Science, vol 60(11), pages 2835-2857. Retreived from: www.nber.org/papers/w17950.

The literature also suggests that sustainability activities of companies can have a positive impact on companies' cost of capital since companies with good sustainability records may be more likely to attract investors due to the expectation of reduced risks. Therefore, Clark et al.'s meta-analysis found that 90% of the studies on the cost of capital indicate that good ESG standards lower the cost of capital for companies.[1418] Similarly, another large meta-study finds that most of the assessed studies show a significant relationship between sustainability performance and the cost of capital.[1419] The cost reduction for equity is estimated by other researchers to be around 1%.[1420]

Sub-option 4.1: Narrow category of business (limited by sector)

The economic benefits for individual companies from an enhanced brand image or reputation can be expected to be positive but smaller if all companies within a whole sector would be liable to a new regulation and would therefore improve their due diligence activities. The relative advantage for a company within the sector vis-à-vis its direct competitors which are following the same standards could be rather small and a company would need to advance its due diligence policies beyond the average of the other companies and the required minimum standards set out in the regulation in order to benefit from reputation effects. However, as described in the general text for option 4, European companies in the selected sector(s) could still benefit from reputational effects vis-à-vis non-European competitors. Similarly, European companies could benefit from a possible first mover advantage in the global market, which may, depending on the industry structure and export dependency of the selected sector(s), be of great economic importance.

Similar to the description under brand image and reputation, potential economic benefits related to the ability to attract and retain human resources for an individual firm within a selected sector could be relatively small vis-à-vis European competitors, unless the company would implement a more ambitious approach than the average of companies. In this case it can be expected that economic benefits could arise from its possibility to attract and attain talent better than its competitors. As described above, European companies may be able to attract better and more international high-skilled labour on the global market if there is a first mover advantage from increased and improved due diligence measures.

The magnitude of economic benefits through better risk management, operational efficiency and innovation from this regulator options depends on the size if the sector and the resulting number of firms to which the regulation applies. The economic benefits resulting from better risk management, operational efficiency and innovation can be experiences independent of whether a company has a relative advantage vis-à-vis its competitors. As a result, the larger is the sector to which the regulation applies, the

[1418] Clark, Gordon L. and Feiner, Andreas and Viehs, Michael (2015). From the Stockholder to the Stakeholder: How Sustainability Can Drive Financial Outperformance. Available at SSRN: https://ssrn.com/abstract=2508281 or http://dx.doi.org/10.2139/ssrn.2508281.

[1419] Gianfrate, G. and Schoenmaker, D. and Wasama, S. (2018). Cost of capital and sustainability: a literature review. Working paper series 03, Erasmus Platform for Sustainable Value Creation, Rotterdam School of Management. Available at https://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=5&cad=rja&uact=8&ved=2ahUKEwjdhZSr3vjhAhVEIVAKHTj8AiwQFjAEegQIBBAC&url=https%3A%2F%2Fwww.rsm.nl%2Ffileadmin%2FImages_NEW%2FErasmus_Platform_for_Sustainable_Value_Creation%2F11_04_Cost_of_Capital.pdf&usg=AOvVaw1Csckr51QrS7OOrmnzFYrH.

[1420] Bliss, R. and Jordan, S. and Rochlin, S. and Yaffe Kiser, C. (2015). Project ROI Report: Defining the Competitive and Financial Advantages of Corporate Responsibility and Sustainability. IO Sustainability, Lewis Institute for Social Innovation at Babson College. Available at https://www.issuelab.org/resource/project-roi-report-defining-the-competitive-and-financial-advantages-of-corporate-responsibility-and-sustainability.html.

more companies are required to take due diligence measures and the more economic benefits can be experienced.

The economic benefits for individual companies from improved stock performance and lower cost of capital would remain the same, but the benefits overall for the economy would be lower since only a selected sub-set of companies would be affected. Concerning the choice of sectors one study found that the relationship between social and environmental policies and stock market and accounting performance is stronger in sectors where companies deal with consumers (B2C) not companies (B2B), where companies compete based on brands and reputations and where products depend on large amounts of natural resources.[1421] This may be kept in mind when formulating a concrete regulatory option of this kind.

Sub-option 4.2: Horizontally across sectors

The potential benefits arising for individual firms from their improved brand image and reputation and from their increased attractiveness for employees may differ depending on the number of firms to which the new regulation applies, as described below.

The economic benefits arising from better risk management, operational efficiency and innovation as well as those created by better stock performance and lower capital cost are expected to be the largest when applying to a large number of companies.

Sub-option 4.2(a): Set of large companies

The extent of potential economic benefits resulting from enhanced brand image and reputation would depend on the number of companies which would be affected by the regulation. In general, if a set of few large companies would be affected by the regulation, it can be assumed that the companies would benefit from improved reputation, especially vis-à-vis other companies which are not following the same standards (i.e. other European companies which are not affected or non-European companies). However, the extent to which sales increase depends on a great number of firm- and sector-level characteristics. The affected large companies are also likely to benefit from a first-mover advantage on the global market.

Similar to the described benefits from brand image and reputation it can be expected that an application of the new regulation to a small set of large companies only would enable individual companies to benefit from their increased ability to attract and retain talent, especially vis-à-vis companies which are not applying the same due diligence standards.

The potential economic benefits under this regulatory option are expected to be smaller than those expected under options 4.1 and 4.2(b) as it would only apply to a small set of large companies.

Similarly, the potential economic benefits are expected to be smaller than those expected under options 4.1 and 4.2(b) as it would only apply to a small set of large companies.

Sub-option 4.2(b): All business, including SMEs

[1421] Eccles, R. G., and Ioannou, I. and Serafeim, G. (2014). "The Impact of Corporate Sustainability on Organizational Processes and Performance," Management Science, vol 60(11), pages 2835-2857. Retreived from: www.nber.org/papers/w17950

It can be expected that the economic benefits for a company resulting from an enhanced brand image and reputation could be relatively small vis-à-vis direct EU competitors if all EU companies would be liable to the new regulation. This could be the case if, as a result, improved due diligence policies and measures by companies would become the norm and the expected standard. In this case companies could probably not experience an enhanced brand image that would translate into higher sales or the willingness to pay higher prices by customers since all companies would be required to have similar minimum standards. A company would then need to go beyond the minimum standards set out in the new regulation and carry out better due diligence in order to have an advantage for its reputation and be able to charge higher prices as a result or sell more.

However, as discussed under the general section for option 4, European companies could still benefit from reputational effects vis-à-vis non-European companies and could experience a first-mover advantage on the global market. The extent to which sales increase depends on a great number of firm- and sector-level characteristics. It should be noted that smaller companies are less likely to financially benefit from reputation-induced benefits. Due to their small size, a reputation-based increase in total sales is less likely to generate additional income sufficient to cover the additional costs that result from new DD requirements.

Table 8.45 exemplarily outlines how additional costs can impact on small companies' income and profitability respectively. As outlined above, it should be noted that these numbers are also hypothetical. We calculated average revenues by sector for all EU28 companies with 10-49 employees. We assumed a general profit margin of 10%, which was applied to all sectors across the board for small EU28-based companies. We also assumed a reputation-induced increase in small companies' sales of 10%. Based on the 10% margin, we calculated companies' ex-ante profits, i.e. profits before the implementation of DD regulation. We then applied annual cost estimates for mandatory DD based on "alternative total costs", which results in small companies' ex-post costs. For the manufacturing sector, for example, a 10% reputation-induced increase in the revenues of companies with 10-19 employees translates to a 34% decrease in companies' average corporate income. A reputation-induced increase in the revenues of manufacturing companies with 20-49 employees translates to a 5% decrease in companies' average corporate income. Accordingly, small companies with relatively low annual revenues might not be able to compensate higher cost by reputation-induced increases in sales and net income respectively. Compared to large companies with relatively high sales volumes, small companies with low profit margins are at a much greater risk of being driven out of business as the reputation-induced increase in sales might not generate income sufficient to cover the additional regulation-induced cost burden.

Table 8.45: Potential impact of mandatory DD on small companies' revenues and profit margins, by sector, approximated annual cost of mandatory DD based on "alternative total costs" (median data)

EU28	Size	Annual revenue/company	Ex ante income at 10% profit margin	Approximate annual cost of mandatory DD, based on "alternative total costs" (median data)	Ex post income at 10% profit margin	Ex post income at 10% profit margin after 10% reputation-induced growth in revenues	Relative change in ex post profits
B Mining and quarrying	10-19	EUR 2,468,810	EUR 246,881	EUR 75,000	EUR 171,881	EUR 196,569	-20%
C Manufacturing	20-49	EUR 7,249,714	EUR 724,971	EUR 100,000	EUR 624,971	EUR 697,469	-4%
D Electricity, gas, steam and air conditioning supply	10-19	EUR 1,715,826	EUR 171,583	EUR 75,000	EUR 96,583	EUR 113,741	-34%
E Water supply; sewerage, waste management and remediation activities	20-49	EUR 4,968,763	EUR 496,876	EUR 75,000	EUR 421,876	EUR 471,564	-5%
F Construction	10-19	EUR 24,522,320	EUR 2,452,232	EUR 75,000	EUR 2,377,232	EUR 2,622,455	7%
G Wholesale and retail trade; repair of motor vehicles and motorcycles	20-49	EUR 37,493,750	EUR 3,749,375	EUR 75,000	EUR 3,674,375	EUR 4,049,313	8%
H Transportation and storage	10-19	EUR	EUR	EUR	EUR	EUR	-20%

		2,535,421	253,542	75,000	178,542	203,896	
I Accommodation and food service activities	20-49	EUR 5,827,666	EUR 582,767	EUR 75,000	EUR 507,767	EUR 566,043	-3%
J Information and communication	10-19	EUR 1,518,408	EUR 151,841	EUR 75,000	EUR 76,841	EUR 92,025	-39%
L Real estate activities	20-49	EUR 4,013,354	EUR 401,335	EUR 75,000	EUR 326,335	EUR 366,469	-9%
M Professional, scientific and technical activities	10-19	EUR 3,921,197	EUR 392,120	EUR 75,000	EUR 317,120	EUR 356,332	-9%
N Administrative and support service activities	20-49	EUR 11,310,863	EUR 1,131,086	EUR 75,000	EUR 1,056,086	EUR 1,169,195	3%

Source: Own approximations based on Business and Stakeholder Surveys.

Similar to the described benefits from brand image and reputation, it could be expected that no or only small benefits would be created related to human resources for individual businesses since all companies would need to implement a similar due diligence standard. However, those companies which would pursue a due diligence practice beyond the average or minimum standard might benefit from a relatively higher attractiveness for employees.

As economic benefits resulting from improved risk management, operational efficiency and innovation do not depend on a relative advantage vis-a-vis competing firms, but all firms can simultaneously benefit from a better risk management and operational efficiency, a broader application of a new regulation would provide more benefits. Since this regulatory option would apply to all companies in the EU, this regulatory option is expected to provide most economic benefits from better risk management, operational efficiency and innovation.

Same as for risk management and operational efficiency this regulatory option would provide most economic benefits from better stock performance and lower capital costs as it would apply to all companies in the EU.

Sub-option 4.2(c): All business plus specific additional obligations only applying to large companies

Depending on the additional obligations and the ability of large companies to communicate their additional achievements regarding the additional obligations to their customers, this option may provide large companies with the possibility to enhance their brand impact and reputation vis-à-vis smaller companies with less due diligence activities. Whether such additional obligations would translate into advantages for their brand image and reputation might also depend on the types of additional obligations and how important these are considered by customers.

As outlined above, the extent to which sales increase depends on a great number of firm- and sector-level characteristics. Generally, the higher companies' additional cost, the more likely a decrease in these companies' net income. Companies with low profit margins could be at risk of being driven out of business if the reputation-induced increase in sales does not generate sufficient income to cover the additional regulation-induced cost burden.

For economic benefits related to human resources, the same considerations apply as those described for brand image and reputation.

Whether additional obligations for large companies would provide additional economic benefits resulting from an improved risk management and better operational efficiency of those companies, depends on the additional obligations. If these would specifically address risk management and matters of operational efficiency, the resulting economic benefits may increase. Additional obligations relating to the Paris Agreement are difficult to see how they would contribute to improving risk management and operational efficiency; however they my potentially help to foster innovation.

Again, whether additional obligations for large companies would provide additional economic benefits resulting from an improved stock performance of lower cost of capital depends largely on the additional obligations and is therefore difficult to assess.

Sub-option 4.3: Sub-options 1 and 2 accompanied by a statutory oversight and / or enforcement mechanism

Having additional enforcement mechanisms in place might increase not only the compliance by companies with the new regulation but also the credibility of their due diligence activities and reporting. This could potentially increase the economic benefits arising from improved brand image and reputation. However, as discussed for option 4.2(b) this would also depend on the set of companies to which the regulation applies and whether the enhanced brand image would provide a competitive advantage vis-à-vis a company's most important competitors.

Similar as for brand image and reputation it can be assumed that any type of enforcement mechanism might increase the due diligence activities taken by companies as well as their credibility vis-à-vis their current and potential future employees. As a result, companies may be better able to attract and retain qualified people and draw economic benefits out of that. Again, it depends on the relative advantages vis-à-vis a company's competitors.

It can be expected that additional enforcement mechanisms would increase the compliance by companies and thereby increase also potential economic benefits from improved risk management and operational efficiency.

Same as for risk management and operational efficiency, it can be expected that additional enforcement mechanisms would increase the compliance by companies and thereby increase also potential economic benefits from better stock performance and lower cost of capital.

The considerations discussed for sub-option 4.3 in general, also apply for the specific sub-options 4.3(a): Mechanisms for judicial or non-judicial remedies and 4.3(b): Sub-option 4.3(b): State-based oversight body and sanction for non-compliance.

3.1.4 Comparison of options and final assessment

Under the status quo (option 1) it is unclear how national regulations will develop and what obligations these will entail for companies and/or whether individual companies might take voluntary initiatives. According to the survey, the greatest economic benefits are expected from greater supply chain certainty (42%), lower operational risks (34%) and greater legal certainty (33%). It is expected that an economic benefit could also be expected if companies advance due diligence activities on their own behalf and succeed to communicate these. These companies could experience benefits in terms of an improved brand image and reputation which may result in higher sales of their products.

For the introduction of new voluntary guidelines (option 2), additional benefits are expected in similar areas as the observed benefits from ongoing activities under option 1. Business respondents to the survey expect additional economic benefits for their companies resulting from increased supply chain certainty (22%), from a greater leverage over non-EU supplier provided by non-negotiable standards (20%) and from lower operational risks (16%). Benefits from improved reputation and brand image will, again, depend primarily on individual companies' actions taken. It is not expected that voluntary guidelines can have a significant impact on these. Similarly, possible economic benefits in areas such as human resources, arising from improved risk management, operational efficiency and innovation or better financial/stock performance and lower capital cost depend on voluntary due diligence actions by companies. Therefore, it is not expected that economic benefits in these areas arise under this policy option.

For the introduction of a mandatory reporting requirement (option 3), survey respondents expect additional benefits in similar areas as for option 2, i.e. benefits in the form of greater supply chain certainty (32%), greater legal certainty (29%), greater leverage over non-EU suppliers provided by a non-negotiable standard (24%) and from lower operational risks (22%). Again, potential economic benefits for firms resulting from mandatory due diligence reporting depend on the extent to which mandatory reporting requirements enact changes in companies' policies. The likelihood can be expected to be higher than for voluntary guidelines since public reporting may provide some incentives to improve company policies and practices on sustainability issues. However, based on experiences from the EU NFRD this effect is expected to remain relatively low. Therefore, economic benefits in the area of human resources, arising from improved risk management, operational efficiency and innovation or better financial/stock performance and lower capital cost are expected to remain low.

Looking at mandatory due diligence requirements (option 4), respondents again expect economic benefits in the same areas: They are mainly expected in the form of greater leverage over non-EU suppliers provided by a non-negotiable standard and greater legal certainty (46% each), followed by greater supply chain certainty (44%) and lower operational risks (35%).

Option 4 could provide significant economic benefits for firms related to their brand image, reputation and sales, if companies will, as a result of the new regulation, increasingly implement due diligence activities and these are known by consumers. Existing studies have shown that sustainability measures can foster the sales of a company's products and allow it to charge higher prices. However, these benefits may be lower if the regulation is applied EU-wide. The reason is that an individual company would not have a competitive advantage from its due diligence activities vis-à-vis other European companies if all companies are taking the same or similar measures. A competitive advantage would then only exist vis-à-vis companies from non-EU countries which are not required to implement due diligence measures.

Similarly, economic benefits in the area of human resources can be expected as sustainability measures and CSR activities can make a company more attractive for job applicants and therefore companies can attract talents even when they do not pay highly competitive salaries.

Economic benefits can also be expected from better risk management, operational efficiency and innovation. Several studies have found that sustainability measures by firms have a positive impact on the company risk and operational efficiency which translates into economic value.

It can also be expected that economic benefits for companies arise in the form of better financial or stock performance and access to lower cost of capital if a new EU regulation requires mandatory due diligence and leads to improved due diligence measures taken by companies. Several studies find a positive relationship between companies' sustainability activities and financial or stock performance. Other studies also suggest that sustainability activities of companies can have a positive impact on companies' cost of capital.

When comparing a company's costs and benefits from due diligence activities it is important to point out that there may be economic benefits which are felt more immediately and can be linked more directly to due diligence measures, such as an improved brand image and reputation, improved governance, transparency and management of supply chains, leading also to reduced operational and strategic company risks. However, there are also economic benefits which may occur in a rather long-term perspective and which may be less directly linked to a company's due diligence activities since they are influenced also by other factors. For example, a more direct benefit in the form of an improved operational knowledge (i.e. deeper knowledge of a company's supply chains and reduced operational and strategic risks) can reduce a company's cost in the long-term by increasing its efficiency and reducing risks and can increase a company's revenue by creating more growth opportunities.

In summary, the total cost that companies face critically depends on the details of the legal requirements. Our estimates generally demonstrate that irrespective of companies' sizes, the costs increase with the escalation of policy requirements. In other words, as expected, more comprehensive DD requirements have a far greater bearing on companies' balance sheets than mere reporting requirements. In such context, while increasing costs could prove detrimental for SMEs, their knowledge of business partners may allow them to reduce costs[1422] as they gain leverage to perform due diligence along their value chain. At the same time, it should be noted that, due to the implementation of efficient DD procedures, e.g. by use of modern tracking technologies, some SMEs may actually face lower relative cost than large companies. Regarding technology solutions, our results show that new tracking technologies and software-supported value chain management systems are likely to simplify DD tasks for companies of all sizes.

Finally, the estimations provided in this section should be considered with caution, as they are based on a limited subset of participants that by no means represent the overall companies' ecosystem at the EU level.

3.2 Impacts on non-Economic spheres: Social, Human Rights and Environmental Impacts, and Impacts on Public Administration

This preliminary impact assessment of regulatory options, focusing on the social, human rights, environmental, and public administration impacts, first provides general remarks and descriptions of each impact area. Thereafter, the four impact areas are analysed in detail for each policy option. Finally, the report presents a global comparison of the policy options, highlighting the most relevant challenges/costs, and opportunities/benefits across areas.

3.2.1 General remarks and description of impact areas

- **Social impacts**

An assessment of social impacts can refer to a broad range of issues which concern possible impacts on society as a whole as well as the well-being of individuals within a society. Therefore, an assessment of social impacts can include impacts on employment and work conditions as well as impacts in broader areas such as education, public health, community welfare or rural development.[1423] The "Guidance for assessing Social Impacts

[1422] Lin, Feng-Jyh, and Yi-Hsin Lin. 2016. "The Effect of Network Relationship on the Performance of Smes". Journal of Business Research 69 (5): 1780-1784. https://doi.org/10.1016/j.jbusres.2015.10.055

[1423] Social impacts are also often closely related to human rights issues, which are assessed in a different section, and some aspects could be discussed as part of both areas of impact – social impacts and human rights impacts. For the purpose of this impact assessment, basic labour rights concerning child and forced labour are discussed as part of social impacts, although these are also key human rights impacts in the context of business activities.

within the Commission Impact Assessment system" refers to six broad impact areas: Employment and labour market; standards and rights related to job quality, social inclusion and protection of particular groups; equality of treatment and opportunities, non-discrimination; social protection, health, social security and educational systems; and public health and safety.[1424]

Which potential social impacts are the most relevant impacts to assess, depends to a large extent on the final content of a new regulation, whether or which areas are specified e.g. in reporting requirements or as part of due diligence requirements, and how enforcement would take place. Existing impact assessments on non-financial reporting requirements and due diligence obligations largely focus on the potential impact on workers and working conditions. However, the impacts on other rights-holders who are not workers are less well-documented.

This is not a full impact assessment of a regulatory proposal. As such, the assessment of social impacts will consider those areas which are expected to be most likely or directly affected by a new regulation. This assessment of social impacts will mainly focus on two aspects which can be related to a potential change in companies' practices: First, it will discuss the potential impacts of the proposed policy options on employment/working conditions[1425] in the EU as well as the possible impacts on work conditions and basic labour rights in third countries. Second, it will discuss potential employment effects in the EU (and possibly third countries) as a result of additional requirements for businesses which may affect their competitiveness.

It is assumed that the first area of social impacts can be linked relatively directly to the possible operational changes enacted by a new regulation for companies. Working conditions are directly affected by company policies and practices, same as basic labour rights in companies' supply chains. Impacts on employment are less direct and influenced by other economic factors. Nevertheless, employment is an important factor to be taken into account and therefore is discussed briefly for each option.

In contrast, the assessment of social impacts will not discuss issues which are rather broadly and indirectly linked to the assessed policy options, such as income distribution, poverty or social inclusion. Impacts on income distribution and social inclusion could likely result from changes in employment and wages in particular sectors, but impacts are rather indirect. Moreover, such broad areas of societal development are simultaneously influenced by various other factors such as the general state of the economy and specific social policies which makes impacts from a new regulation difficult to assess.

In general, most social impact assessments are discussed in a qualitative way as most social impacts are difficult to quantify. This is the case also for most impact assessments concerning similar legislative initiatives (e.g. the EU Impact Assessments on Conflict Minerals, Non-Financial Reporting or on the Timber Regulation). Moreover, since many of

[1424] DG Employment, Social Affairs and Inclusion (2009). Assessing Social Impacts. Ref. Ares (2009) 326974 - 17/11/2009. Available at: https://ec.europa.eu/smart-regulation/impact/key_docs/docs/guidance_for_assessing_social_impacts.pdf.

[1425] The ILO describes working conditions as: "Wages, working time, work organization and conditions of work, arrangements to balance working life and the demands of family and life outside work, non-discrimination and protection from harassment and violence at work are core elements of the employment relationship and of workers' protection, and also affect economic performance. Working conditions cover a broad range of topics and issues, from working time (hours of work, rest periods, and work schedules) to remuneration, as well as the physical conditions and mental demands that exist in the workplace." Source: International Labour Organisation (ILO) (n.a.). Working Conditions. Available at: https://www.ilo.org/global/topics/dw4sd/themes/working-conditions/lang--en/index.htm the national legislative initiatives have only been implemented in recent years, at the time of writing no comprehensive studies on their implementation and possible social impacts exist yet.

- **Impacts on Human Rights**

The human rights impacts section presents an in-depth analysis of the survey responses for each of the four policy options, paying particular attention to fundamental rights of concern including children's rights and freedom from slavery, as well as sectors of concern such as retail, manufacturing, and mining. The analysis draws from the literature review and links it to the survey results that assess stakeholder and company expectations regarding due diligence impacts. The in-depth review of the survey responses focuses on respondent's expectations of the ability of the four policy options to have an impact on human rights. Of particular interest, the analysis distinguishes between stakeholder estimations and self-reported expectations from business representatives. Considering historical links between business and sensitive human rights dimensions, the analysis conducts a sector-specific assessment of company responses. The analysis likewise links evidence of implications of existing but more narrowly limited due diligence requirements, to highlight the unintended consequences that addressing human rights challenges in one region may have on another region.

To assess impacts on children and vulnerable communities, we assess companies' current due diligence practices and the self-reported survey results from their expected impacts of new due diligence regulations. As already noted, the study assumes that specific sectors (such as the case of conflict minerals) and historical contexts mean that some sectors may have developed greater capacity to mitigate impacts on vulnerable communities due to existing standards applicable to their operations and public scrutiny. Considering the wide range of industry representation, the analysis considers the current and past realities of the various sectors in protecting vulnerable persons – for example focusing on the manufacturing and retail sectors' ability to improve due diligence for human rights and environmental impacts. In line with the environmental impact assessment approach that follows, findings were cross-checked against relevant literature.

Companies and stakeholders were first asked to describe the language they employ to refer to their due diligence processes, their current practices and the human rights and environmental aspects covered in their measures. Thereafter, to address options 2 to 4, companies and stakeholders were asked whether they considered that the new regulation was likely to have a social, human rights or environmental impacts. This accounts for their perception about the capacity of the different regulation alternatives to influence implementation of due diligence duties. Additionally, respondents who indicated that the regulation was likely to have impacts on human rights were asked to evaluate the potential impact of each policy option across 19 specific human rights, confirming whether they foresee positive, neutral or negative effects of the specific proposed regulation on each right. These responses allow the researchers to assess specific areas that could either present the greatest opportunities for right-holders or pose the biggest challenges for significant impact.

Due to data limitations, the participants' prospects for the sub-options of the fourth alternative (new regulation requiring mandatory due diligence) are studied considering the general definition of the option. Respondents were presented a general scenario of mandatory due diligence without specifying any enforcement mechanisms or differential conditions according to company size or economic sector concerning human rights impacts, for example.

- **Environmental Impacts**

The process to introduce new regulations with an environmental dimension is not exempted from resistance and frictions among businesses and governments. Alongside transport, the environment has consistently been among the three most challenging sectors in terms of complaints against financial sanctions for infringement of regulations.[1426] The existing guidelines, such as UNGPs and the OECD Guidelines, provide a framework based on protecting and respecting human rights and the environment, as well as mitigating and remedying damages derived from businesses' operations. These aim to ease and improve compliance along supply and value chains, explicitly addressing environmental issues at different levels, including climate-related due diligence and the risks that climate change poses to business.

The environmental impacts section presents an in-depth analysis of the survey responses for each of the four policy options, paying particular attention to environmental and climate-related aspects concerning current due diligence practices, as well as the expectations that companies and stakeholders have regarding new due diligence regulation alternatives.

To address options 2 to 4, companies and stakeholders were asked whether they considered that the new regulation was likely to have an impact on the environment. Additionally, respondents who expected impacts from the new regulations, had to evaluate the potential impact of each policy option across ten environmental areas, indicating whether they expected positive, neutral or negative effects. These evaluations allow identifying specific areas that could be left behind by each alternative, or even negatively influenced according to the perceptions of respondents. Regarding the no policy change scenario, companies and stakeholders described the language they employed to refer to their due diligence processes, their current practices and the environmental aspects covered in their measures.

As mentioned above, the participants' prospects for the sub-options of the fourth alternative (new regulation requiring mandatory due diligence) are studied under the general definition of the option due to data limitations.

- **Impact on legal systems of Member States and public administrations**

This section provides an assessment of the potential costs and benefits for public authorities in EU Member States, and on the EU-level for the European Commission. It is necessary to point out, however, that, as this is only a preliminary study, it is not possible to consider the precise legal implications of a specific regulatory proposal, and that regulatory mechanisms in this area are new and rare. It is therefore not possible to estimate the final impact of the policy options analysed in this study. The discussion by policy option mainly serves to highlight factors that may need to be taken into account when a regulatory proposal is formulated, and its impacts are tested with stakeholders.

[1426] Smith, Melanie. 2018. "Challenges in the Implementation of EU Law at National Level". European Parliament. Retrieved from:
http://www.europarl.europa.eu/RegData/etudes/BRIE/2018/608841/IPOL_BRI(2018)608841_EN.pdf

In particular, the discussion of impacts on public authorities outlines several potential cost factors and their likely magnitude. It will also outline the potential benefits, which would need to be reflected upon and assessed in more detail when the regulatory options are defined in more detail, as part of the full impact assessment required if a regulatory proposal were to be formulated.

The following discussion of impacts is based mainly on previous impact assessments of similar legislation, which includes certain national laws discussed in the Regulatory Review. In the stakeholder survey, respondents addressed two questions about the potential impacts on public authorities. It should be noted that almost all respondents stated that they were unable to indicate any costs as these would depend on the scope of the precise legal implications of a potential regulatory mechanism. Therefore, it was considered "impossible to measure without more concrete scope or definitions".[1427]

The introduction of a new regulation on human rights and environmental due diligence could lead to different costs arising from an additional administrative burden for public authorities in EU Member States as well as on the EU level. This includes, for example, costs related to guidance on the implementation of the new regulation, communication activities, monitoring activities to supervise and assess the implementation of the regulation, such as sample reviews and inspections of companies, enforcement in case of non-compliance, as well as judicial costs. Significant additional costs will be created whenever new bodies and institutional structures will need to be set up.

In general, it is not expected that a new regulation on human rights and environmental due diligence would provide apparent economic benefits for public authorities in EU Member States or at the EU level. Economic benefits for public authorities in EU Member States could only arise if it was more efficient to have an EU-wide regulation and EU Member States would, as a result, not advance similar individual legislative initiatives which would create an administrative burden for Member States which would exceed that of a new EU-wide regulation.

3.2.2 Assessment of impacts by policy option

- **Option 1: No policy change**

Social Impacts

The development of the current baseline scenario depends largely on the different policies which EU Member States will advance and implement in the coming years. As described in the section on Regulatory Options, due diligence requirements have already been introduced or proposed in some EU Member States (e.g. France, Germany, UK) and it is expected that due diligence requirements will increasingly be introduced by EU Member States and countries outside of the EU. However, without knowing the precise scope of such national initiatives and whether these include legally binding requirements for companies, social impacts are difficult to assess.

<u>Work conditions and labour rights</u>

If EU Member States increasingly introduce, on a national level, mandatory due diligence laws with a comprehensive coverage including social aspects such as work conditions or

[1427] See the Survey Results presented in the Annex.

labour rights, it can be expected that these laws could have positive effects for the workforce in the EU as well as in third-countries if the application of such laws extends to the whole supply chain. If EU Member States introduce national laws which are less binding and/or have a smaller coverage of issues the expected social impact on employment conditions in the EU and supplying countries would be smaller, although there would still be an improvement compared to not taking any action.

Employment

It can be assumed that this option would not have an impact on employment levels, either in the EU or in third countries. The reason is that the current status quo is not expected to lead to any differences in the production volumes of EU companies and the number of employed people. However, this depends on how national legislation will develop.

Having different national legal frameworks in different Member States could potentially lower any positive social impacts from due diligence requirements if national laws are designed in a way where the law of one Member States contains less strict due diligence requirements than another Member States. This could incentivise a large company to (re)organize its corporate structure in such a way that it would avoid liability in another Member State which poses more demanding requirements.

Human rights and environmental impacts

This section shows the current situation of due diligence processes related to human rights and the environment, focusing on actions carried out by companies in order to prevent, mitigate or remedy potential adverse consequences of their operations.

According to the literature, one of the key achievements of the UNGPs has been to shift the approach to business and human rights from a retrospective liability for corporate violations to a proactive one designed to prevent adverse human rights impacts via due diligence. The results below show the presence of human rights and environmental language in due diligence processes, confirming the shift towards proactive efforts. However, there are also discrepancies between levels of stakeholder perception of human rights and environmental language in due diligence processes: stakeholder respondents declare the use of a human rights or environmental language more often than companies, with gaps that range from 5% to 25%. Also, the actual levels of due diligence practices confirmed by companies may demonstrate gaps in transparency or coherence, as the practices that take place –based on companies' responses– do not match the results for the kind of language that is employed or whether certain measures are expressly included.

The latter –a gap in transparency or coherence– is more likely. Regarding different types of human rights and environmental due diligence areas, the survey shows that 70.85% of companies claim to have undertaken human rights and environmental due diligence compared to the 46.6% that use direct human rights language to classify due diligence practices. Moreover, both survey respondents demonstrated vagueness of due diligence language as a significant proportion suggested that companies use the denomination "Sustainability Due Diligence" or other language to describe their processes (according to 66.7% of mentions by stakeholders and 32.4% of mentions by companies). Thus, discrepancies between actual practices and the language that is used to describe them may lead to under/overestimate due diligence actions performed by companies.

On the other hand, the literature proposes the possibility of corporations passing the burden of due diligence down the supply chain.[1428] Existing studies on supply chain practices indicate that such contractual clauses are often equated with supply chain due diligence practices. In this context, the frequency of vague language or other alternatives to describe human rights or environmental due diligence could likewise demonstrate instances where companies have not themselves established specific human rights or environmental due diligence frameworks, but contract suppliers that have established such practices down the supply chain. However, insofar as not much data exists on how companies classify and label their specific practices, the analysis can only be speculative.

The responsibilities of business enterprises are defined in Guiding Principle 13,[1429] which establishes that business enterprises have a responsibility to: avoid causing or contributing to adverse human rights impacts through their own activities; seek to prevent or mitigate human rights impacts that are directly linked to their operations, products or services by their business relationships, even if they have not contributed to those impacts.

As such, according to the literature, the analogy between the 'corporate responsibility to respect' in the second pillar of the UN Guiding Principles and the tort of negligence in domestic jurisdictions[1430] represents possible opportunities for rights-holders to draw on. Considering the usefulness of the UNGPs due diligence standard as a legal standard of care[1431], there may be direct opportunities for rights-holders who suffers harms as a result of companies' failure to exercise due care. However, despite these similarities with the legal standard of care, the country reports of this study show that there are very few examples of cases where the UNGPs or its due diligence expectations were successfully relied on by claimants to demonstrate binding legal obligations.

In the areas of labour rights, health and safety, and non-discrimination and equality may present the greatest opportunities to meet human rights standards as 87%-95% of companies responded they clearly state such human rights aspects as a matter of their due diligence practices, as well as some form of environmental due diligence. It is noted that these areas are already, for the most part, highly regulated as domestic level. In many case, these domestic laws also provide those affected with statutory remedies. This suggests a strong consistency between corporate practices and regulation, insofar as the areas where most companies are already undertaking due diligence are the areas where laws already impose liability if harms were to take place.

Finally, regarding climate-related issues, the limited use of the term "climate change due diligence", as well as the low proportion of exclusive environmental/climate change due diligence practices (7%), show that the companies are not currently undertaking free-standing or exclusive environmental and climate-related due diligence. Conversely, a greater proportion of companies declare that they explicitly mention climate change

[1428] Jonathan Bonnitcha, Robert McCorquodale, The Concept of 'Due Diligence' in the UN Guiding Principles on Business and Human Rights, European Journal of International Law, Volume 28, Issue 3, August 2017, Pages 899–919. Retrieved from: https://doi.org/10.1093/ejil/chx042

[1429] Ibid.

[1430] Sanders, Astrid, The Impact of the 'Ruggie Framework' and the United Nations Guiding Principles on Business and Human Rights on Transnational Human Rights Litigation (June 23, 2014). LSE Legal Studies Working Paper No. 18/2014. Retrieved from: https://ssrn.com/abstract=2457983

[1431] Aftab, Yousuf. "The Intersection of Law and Corporate Social Responsibility: Human Rights Strategy and Litigation Readiness for Extractive-Sector Companies." *Proceedings of 60th Annual Rocky Mountain Mineral Law Institute* (2014): 19-1. Retrieved from: https://www.business-humanrights.org/sites/default/files/documents/YAftab-Rocky%20Mountain%20Final%20%282014%29.pdf among the environmental aspects covered through due diligence (60%). This result shows that despite not using climate change language to refer to more general due diligence processes/actions, climate change is a specific concern among companies. Also, a considerable proportion of companies include climate implicitly (40%), indicating that climate-related actions are conceptualised as a sub-aspect of environmental due diligence.

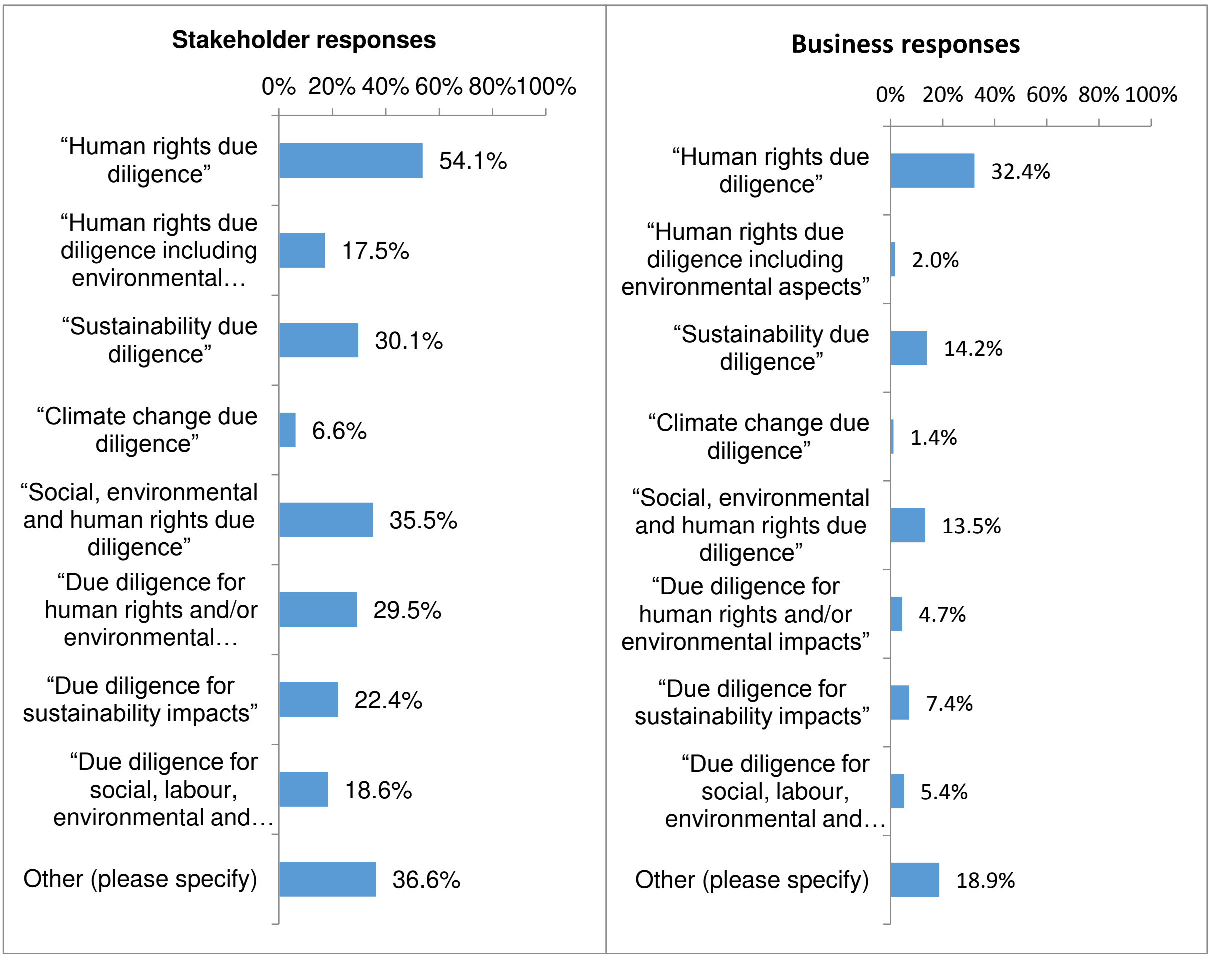
Due diligence language referring to human rights and the environment

Both human rights and environmental concerns are extensively present in the language used to describe due diligence processes.

Regarding human rights terminology, the majority of stakeholders noted that companies describe their due diligence processes as "Human Rights Due Diligence" (54%), and the majority of businesses likewise confirmed that they describe their due diligence processes as "Human Rights Due Diligence" (32%). Thereafter, the second and third most used language of the given options for due diligence processes are "Social, Environmental and Human Rights Due Diligence" (according to 36% of stakeholder respondents, and 14% of business respondents) and "Sustainability Due Diligence" (according to 30% of stakeholder respondents and 14% of business respondents). However, 37% of stakeholders and 19% of businesses noted that companies use other language to describe their processes.

In the case of environmental terminology, descriptions often include language involving environmental aspects linked to human rights and social impacts, among both stakeholders (19% - 36%) and companies (5% - 14%). "Sustainability" is also a term to refer to due diligence processes in both types of participants, although stakeholders perceive it to be more frequently used (22% - 30% among stakeholders) than companies use it to describe their own practices (7% - 14% among companies). A noteworthy finding is that climate change is the least commonly employed denomination among both types of actors (7% for stakeholders and 1% for companies).

Figure 8.8: Due diligence language referring to human rights and environment



Q12 Business Survey; 148 responses – Q10 Stakeholder Survey; 183 responses.

<u>Current practices</u>

Regarding current due diligence processes carried out by companies, near 78% of companies have undertaken due diligence for human rights or environmental impacts. A significant portion of companies (34%) carry out due diligence in specific areas related to human rights, which may or may not include environmental issues. Only 7.4% indicate that they have carried out exclusive environmental or climate change due diligence activities without extending them to other human rights. Overall, most companies (37%) indicated that they undertake due diligence involving all human rights (including environment).

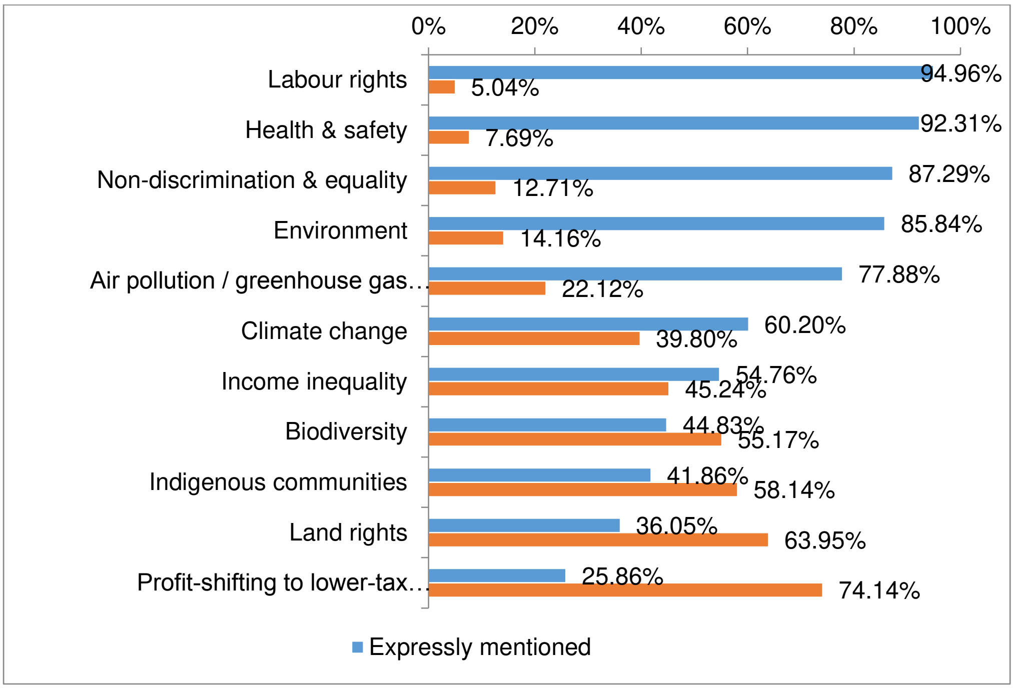
Table 8.46: Current human rights and environmental due diligence practices

Answer Choices	Business
Human rights due diligence, but only in certain areas (for example health & safety, labour, non-discrimination & equality, environmental, land rights & indigenous communities)	33.71%
Human rights due diligence which takes into account all human rights (including environment)	37.14%
Environmental/climate change due diligence (not extending to other human rights)	7.43%
My company does not / has not yet undertaken any form of due diligence for any human rights or environmental impacts	7.43%
Do not know	14.29%
Q10 Business Survey; 175 responses.	

Human rights and environmental aspects covered by companies' due diligence

Both human rights and environmental aspects are perceived by companies to be expressly or implicitly included in their due diligence processes. Labour rights, health and safety, non-discrimination and equality, and income inequality are those that are more often (55% - 95%) stated as expressly included within due diligence. Land rights, indigenous communities, and progressive profit-shifting appear more frequently (58% - 74%) as implicit aspects of due diligence. Regarding the environment, climate change, air pollution or greenhouse gas emissions, and the environment in general are those that more often (60% - 86%) are stated to be expressly included in due diligence. Biodiversity appears more frequently (55.2%) as an implicit aspect of due diligence.

Figure 8.9. Human rights and environmental aspects covered by companies' due diligence



Q11 Business Survey; 133 responses.

Impacts on Public Authorities

As described in the Regulatory Review, due diligence requirements have already been introduced or proposed in some EU Member States (e.g. France, Germany, and UK). It is expected that mandatory due diligence requirements will increasingly be introduced or at least considered by some EU Member States and outside of the EU, but that not all Member States will introduce similar laws or any laws at all.

Unfortunately, it cannot reasonably be predicted what the scope and coverage of these different types of national legislation will be, i.e. what it would cover in terms of issues, companies or sectors, and whether it would be mandatory or voluntary, etc. Therefore, it is not possible to provide precise cost estimates for measures that follow the status quo at national level and assess what administrative burden would be created for public authorities in EU Member States.

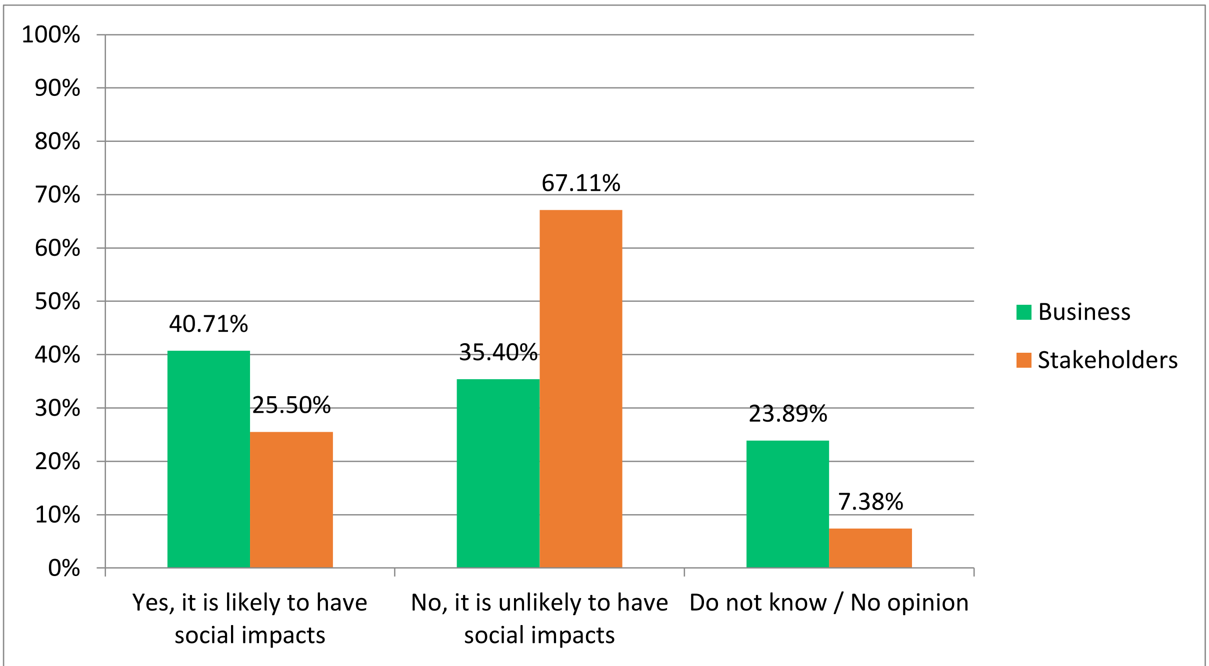
It can be assumed that a situation in which different Member States apply different laws with different requirements and a different scope could create an administrative burden at the EU level, as EU bodies may need to follow and monitor national initiatives and possibly facilitate some type of information exchange. However, it can be expected that this would be covered by existing operational structures and budgets since this would be a normal process of monitoring policy developments in Member States.

- **Option 2: New voluntary guidelines / guidance**

Social Impacts

The results from the online survey reveal different perceptions among the different stakeholder groups regarding the possible social impacts from option 2:[1432] While a large majority of stakeholder respondents (67%) expects no social impacts from new voluntary guidelines, only 35% of the business respondents think that there would not be any social impacts. In contrast, 26% and 40% of the stakeholder respondents and business respondents, respectively, think it is likely that such new guidelines would have a social impact. This indicates that business stakeholders may have a more positive expectation about the potential impacts of new voluntary guidelines compared to general stakeholders. Looking at different sub-groups of respondents within the stakeholder group, 45% of respondents from civil society/NGOs and 9% of respondents from industry organisation expect no social impacts from new voluntary guidelines. In contrast, only 8% and 22% of each group (civil society and industry organisations, respectively) expect positive social impacts.

Figure 8.10: Expected social impacts for Option 2



Q25 Business Survey; 113 responses – Q20 Stakeholder Survey; 149 responses.

Work conditions and labour rights

[1432] Question 25 from Business Survey and Question 20 from Stakeholder Survey. For the full results please see the Annex.

The potential impacts on working conditions in the EU and non-EU countries for this option depend on the extent to which due diligence measures will be implemented as a result of new voluntary guidance. There is already a large amount of existing regulation and guidance on basic labour rights and/or working conditions. The more detailed and implementable the new voluntary guidance is, the higher is the likelihood that firms will follow the standards set out in the guidelines and consider described problems or employ suggested approaches. In general, however, it is expected that this option does not have any impact or – if at all - a very small social impact since such new guidelines would remain voluntary and there is already a large amount of binding law at both national and international level as well as international standards and voluntary guidance in this area (such as by the International Labour Organisation) which firms can take into account.

Expected positive social impacts

When asked in the survey about different areas of social impacts and whether positive, negative or no impacts were expected from introducing new voluntary guidelines, both groups revealed similar expectations. It has to be noted, however, that only those respondents who indicated that the option is likely to have social impacts or had no opinion on this were asked a more detailed question about which social impacts. As a result, only 18% of all stakeholder respondents answered this question at all, and thus the results have to be read with reservations since they may not necessarily be representative of the views of all participants in the survey. Moreover, it is important to keep in mind that respondents were surveyed on the basis of general questions without details about the elements of each option.

The two main areas where mainly positive impacts were expected were related to child labour and forced labour: 73% of stakeholder respondents and 60% of business respondents expect mainly positive impacts from this option for the effective abolition of child labour and 71% and 59%, respectively, expect positive impacts for the elimination of all forms of forced or compulsory labour.

In relation to broader social impacts and impacts related to work and employment conditions, the areas where expectations for positive impacts were highest were the elimination of discrimination in respect of employment and occupation (59% of business respondents, 61% of general stakeholders), improvements on the freedom of association and effective recognition of the right to collective bargaining (52% of business respondents, 50% of general stakeholders) and general improvements on employment conditions/the quality of jobs (50% of business respondents, 52% of general stakeholders). The third category of impacts where general stakeholders expect positive impacts (51% of non-business stakeholders) are improvements regarding the transition from informal to formal employment.

Table 8.47. Overview of the main areas of social impact where positive impacts are expected (Option 2)

Social Impact	Expectation of positive impact (rather than neutral or negative)	
	Business respondents	***General stakeholders***

Effective abolition of child labour	73%	60%
Elimination of all forms of forced or compulsory labour	71%	59%
Elimination of discrimination in respect of employment and occupation	59%	61%
Freedom of association and effective recognition of the right to collective bargaining	52%	50%
Quality of jobs	50%	52%
Transition from informal to formal employment	43%	51%
Q26 Business Survey; 61 responses – Q21 Stakeholder Survey; 45 responses.		

Employment

For the same reasons as described in option 1, it is expected that the introduction of new voluntary guidance would not have an impact on employment levels. It is not expected that such guidelines would have a negative impact on EU production volumes and therefore no negative impact for EU employment levels (nor for employment levels in third countries) is expected. The introduction of new guidelines could potentially create some new jobs in the field of CSR if a company specifically hires someone to implement such guidelines. However, it can be expected that this effect would be very small since companies interested in pursuing voluntary CSR activities will already have specialised staff for CSR activities and familiarisation with an additional guideline can be expected to be covered with existing structures and staff.

Concerning the number of jobs both groups of respondents mainly expect a neutral impact from the introduction of new voluntary guidelines (48% of business respondents, 66% of general stakeholders), i.e. they do not expect any impact.

Impacts on Human Rights

The potential impacts on human rights for this option depend on the extent to which companies will adopt due diligence as a result of new voluntary guidance. While voluntary, there is significant literature that speaks to the possibilities of reputational pressures for companies to comply with voluntary due diligence. For example, the EU Assessment of Due Diligence Compliance Cost, Benefit and Related Effects on Selected Operators in Relation to the Responsible Sourcing of Selected Minerals (2014)[1433] found

[1433] See European Commission (2014), Impact Assessment Accompanying the document Proposal for a Regulation of the European Parliament and of the Council setting up a Union system for supply chain due diligence self-certification of responsible importers of tin, tantalum and tungsten, their ores, and gold originating in conflict-affected and high-risk areas. PART 1 (Impact Assessment). Available at: https://eur-lex.europa.eu/resource.html?uri=cellar:b05a9c8f-a54d-11e3-8438-01aa75ed71a1.0001.01/DOC_1&format=PDF

that as voluntary certification based on OECD Guidance can be expected to have indirect benefits for rights holders as it would encourage demand for ethically and legitimately sourced minerals. This demand can escalate and lead to formalised mining sectors, more sustainable development and benefits for local communities.

Below we present the perceptions of companies and stakeholders regarding general and specific human rights impacts of the implementation of new voluntary guidelines.

The majority of both stakeholders and companies foresee that the new voluntary guidelines are likely to have positive impacts. While over 60% of stakeholders predict most positive impacts to focus on the rights of the child, the rights of indigenous persons, the right to physical/mental health, to not be subject to torture, and the right to non-discrimination/equality, companies predict impacts on their supply chain could most likely regard the right to non-discrimination/equality (71%), the right to life, liberty and security of person (69%), and the right to physical/mental health (67%). Interestingly, the two human rights duties where both stakeholders and companies foresee most positive impacts of voluntary guidelines are in line with those that are most often already perceived by business respondents as *expressly covered* by companies' due diligence processes: health and safety and non-discrimination and equality (section 3.1.3). As these areas are highly regulated already, these findings suggest that new voluntary guidance will simply inform and improve companies' due diligence practices which they are carrying out in response to existing laws. However, those areas mentioned as *implicitly* included in due diligence processes*,* were also foreseen by the majority of stakeholders and companies to be subject to a likely positive impact, although to a lesser degree. While voluntary due diligence mechanisms do not, by themselves, create new law, there are nevertheless legal risks stemming from the adoption or introduction of voluntary guidance. (Lindsay et al. (2013).

As such, it is not surprising that very few respondents expected new voluntary guidelines to have a negative rather than positive impact on human rights. Notably, the highest number of respondents that foresaw a negative impact are companies, expecting negative impacts on the Right of the Child (6.7%) and Women's Rights (6.7%). However, guiding principles risk providing companies with procedural rather than operational leverage to comply with human rights norms. As an example described in the Regulatory Review, the largest gold mine in Latin America, led by a Canadian company, shows policy commitment to human rights norms and due diligence requirements, but continues to be a cause of negative human rights impacts in the city of Paracatu, Brazil[1434]. While the company adheres to international guidance on human rights, local communities still claim to be impacted by health, infrastructural and environmental damages. According to Turke, this demonstrates that without support from the company complying with the requirements, and the proper institutional infrastructure to allow affected rights-holders to seek remedy from a company, mandatory due diligence is in fact at risk of not achieving its intended impacts.

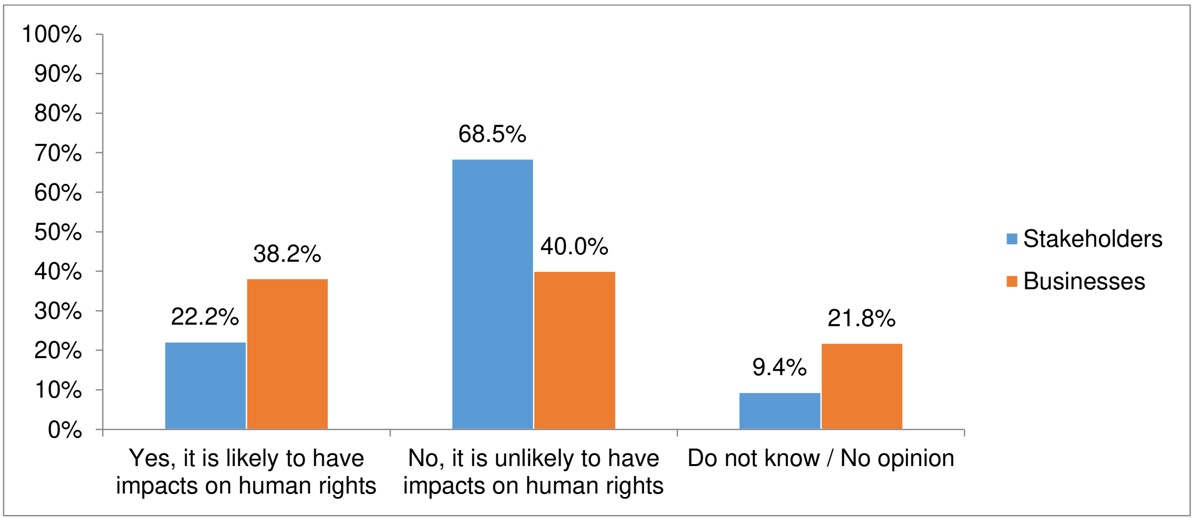
Expected human rights impacts

The majority of stakeholders considered it unlikely that new voluntary guidelines on due diligence through the supply chain would have any human rights impacts (68.5%). Only

[1434] Ibid.

22.2% of stakeholders foresee that the voluntary guidelines on due diligence are likely to have an impact on the enjoyment of human rights. The remaining subset of stakeholders (9.4%) did not know or did not have an opinion regarding the likelihood that new voluntary guidelines impact (or not) human rights. The majority of companies also foresee that it is unlikely that new voluntary guidelines on due diligence through the supply chain would have any human rights impacts (40%). However, the percentage of businesses that believe that it is likely that such guidelines could have an impact on human rights follows closely behind at 38.2%. Nevertheless, almost one in four companies (21.8%) is not able to say whether voluntary new guidelines would have human rights impacts or not. Both types of respondents differ most notably in their expectations that impacts on human rights are unlikely.

Figure 8.11: Expected human rights impacts



Q29 Business Survey; 110 responses – Q24 Stakeholder Survey; 149 responses.

<u>Specific impacts by human rights area</u>

Most stakeholder respondents considered that new voluntary guidelines could have positive impacts on global value chains regarding the right to life, liberty and security of person as well as on freedom from slavery (67% respectively). Additionally, over 60% of respondents foresee positive impacts on the rights of the child, the rights of indigenous persons, the right to physical/mental health, to not be subject to torture, and the right to non-discrimination/equality. The areas where most stakeholders expect neutral impacts are the rights to own property (55%), to freedom from arbitrary arrest (47.5%), and to education (45%). Very few (0% to 5%) of respondents expect a negative rather than positive or neutral impact.

In regards to companies, respondents indicated that new voluntary guidelines could have positive impacts on their supply chain regarding the right to non-discrimination/equality (71%), the right to life, liberty and security of person (69%), and the right to physical/mental health (67%). Over 60% of respondents expect positive impacts on the rights of the child, the right to freedom from slavery and to peaceful assembly/association. Similar to stakeholder respondents, the areas where most companies foresee neutral impacts are the right to own property, to freedom from arbitrary arrest, and the right to education. Very few (0% to 6%) of respondents expect a negative impact, rather than a positive or neutral impact.

Table 8.48: Specific impacts by human rights area

	Stakeholders				Businesses			
	Negative	Neutral	Positive	No opinion / don't know	Negative	Neutral	Positive	No opinion / don't know
Right to Life, Liberty and Security of Person	2.56%	17.95%	66.67%	12.82%	2.22%	20.00%	68.89%	8.89%
Right to Physical / Mental Health	2.56%	25.64%	61.53%	10.26%	2.22%	22.22%	66.66%	8.89%
Right to not be subject to Torture	2.56%	25.64%	61.54%	10.26%	2.17%	26.09%	58.70%	13.04%
Right to Freedom of Opinion/Expression	5.00%	37.50%	45.00%	12.50%	2.22%	35.56%	55.56%	6.67%
Right to Non-Discrimination / Equality	5.00%	25.00%	60.00%	10.00%	4.44%	17.78%	71.11%	6.67%
Right to own Property	2.50%	55.00%	22.50%	20.00%	2.22%	48.89%	37.78%	11.11%
Right to freedom from Slavery	2.56%	20.51%	66.66%	10.26%	4.44%	22.22%	64.45%	8.89%
Right to Freedom from Arbitrary Arrest	2.50%	47.50%	25.00%	25.00%	4.44%	42.22%	35.55%	17.78%
Right to Privacy	5.00%	47.50%	30.00%	17.50%	4.44%	31.11%	48.89%	15.56%
Right to Peaceful Assembly / Association	5.00%	32.50%	42.50%	20.00%	2.22%	31.11%	60.00%	6.67%
Right to Education	2.50%	45.00%	37.50%	15.00%	4.44%	40.00%	44.45%	11.11%
Rights of the Child	2.56%	23.08%	64.10%	10.26%	6.66%	20.00%	62.22%	11.11%
Women's Rights	5.00%	25.00%	57.50%	12.50%	6.66%	17.78%	66.67%	8.89%
Rights of Indigenous Persons	5.00%	22.50%	62.50%	10.00%	4.44%	26.67%	55.55%	13.33%
Rights of People with Disabilities	5.00%	27.50%	52.50%	15.00%	4.26%	21.28%	57.45%	17.02%
Q25 Stakeholder Survey; 41 responses.					**Q30 Business Survey; 47 responses.**			

Environmental Impacts

The potential environmental impacts this option depend on the extent to which companies will adopt due diligence as a result of new voluntary guidance. In line with the reasoning behind positive impacts for rights holders, there is likewise significant literature that speaks to the possibilities of reputational pressures for companies to comply with voluntary due diligence for environmental protection. Identical findings as those for the human rights analysis resulted from the EU Assessment of Due Diligence Compliance Cost, Benefit and Related Effects on Selected Operators in Relation to the Responsible Sourcing of Selected Minerals (2014)[1435] when assessing potential for voluntary guidance to impact environmental sustainability. The study found that voluntary certification based on OECD Guidance would have indirect positive environmental impacts based on reputation as this option would encourage demand for sustainably sourced minerals, leading to formalised mining sectors, more sustainable development and environmental protection. Below we present the perceptions of companies and stakeholders regarding general and specific environmental impacts of the implementation of new voluntary guidelines as conveyed through the online survey.

A large proportion of stakeholder respondents foresee that the new voluntary guidelines are unlikely to have environmental impacts. On the other hand, companies are more evenly distributed between the different expectation options, showing a high level of uncertainty. Voluntary guidelines that address human rights and environmental issues are already available (e.g. the OECD Guidelines, and Guidance on Climate-related Information[1436]). However, new voluntary guidelines by their nature are unlikely to be legally binding or enforceable. Taking this into account, the participants' expectations are consistent with their evaluation of the current situation, i.e. an extended need for a common regulation.

Stakeholders and companies who foresee environmental effects identify similar areas that are likely to have positive impacts. The most relevant is environmental air pollution, followed by waste, water resources and greening of the economy. Areas where respondents show diverging expectations are energy use and mix, and forests. Again, companies show more uncertainty regarding specific impacts, probably because some of them are beyond the scope of their business operations, or the knowledge of the individual respondent.

The uncertainty and low expectations regarding the impact of new voluntary guidelines on the environment coincide with the warnings issued on the Report of the Special Rapporteur on extreme poverty and human rights, 'Climate change and poverty'[1437], which states that overreliance on voluntary private sector efforts could lead to an extremely unequal situation regarding the consequences of climate change. The report stresses that while there is no doubt that corporate actors must play a role in providing and implementing solutions to climate change, they are not likely to be capable of

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[1435] See European Commission (2014), Impact Assessment Accompanying the document Proposal for a Regulation of the European Parliament and of the Council setting up a Union system for supply chain due diligence self-certification of responsible importers of tin, tantalum and tungsten, their ores, and gold originating in conflict-affected and high-risk areas. PART 1 (Impact Assessment). Available at: https://eur-lex.europa.eu/resource.html?uri=cellar:b05a9c8f-a54d-11e3-8438-01aa75ed71a1.0001.01/DOC_1&format=PDF

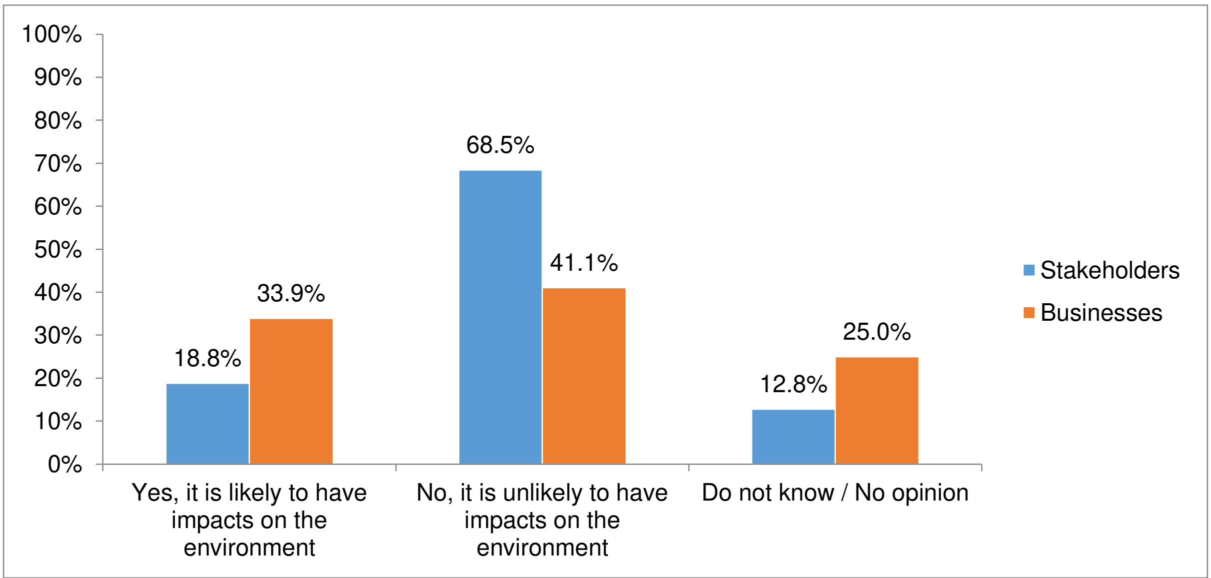
[1436] European Commission. 2019. "Guidelines on Reporting Climate-Related Information". Brussel. Retrieved from: https://ec.europa.eu/finance/docs/policy/190618-climate-related-information-reporting-guidelines_en.pdf

[1437] Office of the United Nations High Commissioner for Human Rights. 2019. "Report of the Special Rapporteur on Extreme Poverty and Human Rights. Climate Change and Poverty." Retrieved from: https://www.ohchr.org/EN/HRBodies/HRC/RegularSessions/Session41/Documents/A_HRC_41_39.docx promoting a comprehensive approach that ensures the conditions necessary for climate change mitigation.

Expected environmental impact

Most general stakeholders considered it unlikely that new voluntary guidelines on due diligence through the supply chain would have any environmental impact (69%). Only 19% of general stakeholders foresee that the voluntary guidelines on due diligence are likely to have an impact on the environment. The remaining subset of general stakeholders (13%) did not know or did not have an opinion regarding the likelihood that new voluntary guidelines impact (or not) the environment. Most companies also foresee that it is unlikely that new voluntary guidelines on due diligence through the supply chain would have any environmental impact (41%). Nonetheless, the percentage of businesses that believe that it is likely that such would guidelines have an impact on the environment is at 34%. Finally, one in four companies (25%) is not able to say whether voluntary new guidelines would have environmental impacts or not.

Figure 8.12: Expected environmental impacts under Option 2



Q27 Business Survey; 112 responses – Q22 Stakeholder Survey; 149 responses.

Specific impacts by environmental area

Both stakeholders and companies considered that the new voluntary guidelines could have positive impacts on their global value chains regarding environmental air pollution (61% - 63%). Also, more than 50% among both actors expect positive impacts on waste, water resources and greening of the economy. The areas where stakeholders and companies have diverging expectations regarding positive impacts correspond to energy use and mix (43 versus 54% respectively) and forests (55% versus 45% respectively). Uncertainty regarding the impacts on different areas is higher among companies that in stakeholders, more than 20% of companies declare that they do not know or have no opinion on potential impacts.

Table 8.49: Specific impacts by environmental area

	Stakeholders				Businesses			
	Negative	Neutral	Positive	No opinion / don't know	Negative	Neutral	Positive	No opinion / don't know
Environmental Air Pollution	0.0%	15.0%	62.5%	22.5%	2.0%	16.3%	61.2%	20.4%
Waste	0.0%	22.5%	57.5%	20.0%	2.0%	18.4%	59.2%	20.4%
Energy use and mix	0.0%	40.0%	42.5%	17.5%	2.1%	22.9%	54.2%	20.8%
Transport	0.0%	27.5%	55.0%	17.5%	2.0%	34.7%	42.9%	20.4%
Water Resources	0.0%	22.5%	57.5%	20.0%	2.0%	22.5%	57.2%	18.4%
Biodiversity	2.5%	30.0%	50.0%	17.5%	2.0%	30.6%	44.9%	22.5%
Agricultural Fertilisers	7.5%	20.0%	55.0%	17.5%	2.0%	20.4%	49.0%	28.6%
Forests	2.5%	25.0%	55.0%	17.5%	2.0%	24.5%	44.9%	28.6%
Fisheries	2.5%	32.5%	40.0%	25.0%	0.0%	28.6%	38.8%	32.7%
Greening of the Economy	2.4%	19.5%	51.2%	26.8%	2.0%	22.0%	50.0%	26.0%
Q23 Stakeholder Survey; 41 responses.					**Q28 Business Survey; 50 responses.**			

Impacts on public authorities

A potential cost which may arise for public authorities is the cost of drafting the new guidelines and communicating it at the EU and national levels. Depending on the aspired content and scope of the new guidelines, an external study may be necessary, which based on the costs of a similar study is estimated at a cost of 200,000-300,000 EUR.[1438] In the Impact Assessment regarding the EU Conflict Minerals Regulation it is estimated that the cost of promoting a new communication via national contact points and the Enterprise Europe Network (EEN) is equivalent to 0.05 full-time equivalent (FTE).[1439] It is not possible to estimate the precise figures in Euros of salary expectations based on available data. Moreover, the exact costs of the 0.05 FTE estimation would depend on the level of expertise required from the person(s) in post. In this, regard, it is noted that the Conflict Minerals Regulation applies only to limited issues in a limited sector, and that more time may be required if the due diligence requirements applies to a larger set of companies and sectors. Due to their voluntary nature, new voluntary guidelines are unlikely to be legally binding or enforceable. As a result, there are no additional costs expected for the judicial system.

- **Option 3: New regulation requiring due diligence reporting**

Social Impacts

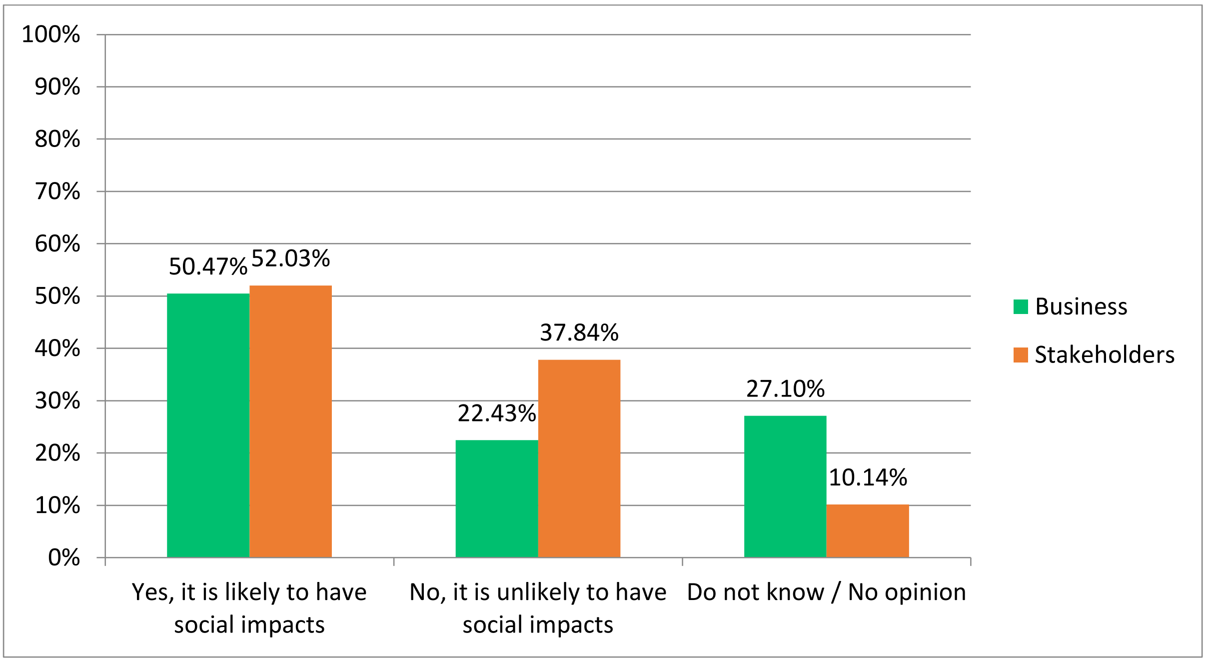
Survey results show that half of both groups of stakeholders do expect social impacts from an introduction of mandatory reporting requirements on due diligence through the supply chain[1440]: 52% of non-business stakeholders and 50% of the business respondents think that there would be a social impact from new reporting requirements on due diligence. Only 38% of non-business stakeholders and 22% of business respondents do not expect any social impacts. Looking at different sub-groups of stakeholders, 24% of respondents from civil society/NGOs and 20% of respondents from industry organisation expected social impacts from this regulatory option, while 29% and 5%, respectively, did not expect any social impact. However, it has to be pointed out that the large majority of both groups (44% and 66%) did not respond to this question.

[1438] See European Commission (2014), Impact Assessment Accompanying the document Proposal for a Regulation of the European Parliament and of the Council setting up a Union system for supply chain due diligence self-certification of responsible importers of tin, tantalum and tungsten, their ores, and gold originating in conflict-affected and high-risk areas. PART 1 (Impact Assessment). Full external report available at https://publications.europa.eu/en/publication-detail/-/publication/dced6d04-92fb-4a20-a499-4dad9974aee7 01aa75ed71a1.0001.01/DOC_3&format=PDF

[1439] A full-time equivalent (FTE) is a unit to measure employed persons in a way that makes them comparable although they may work a different number of hours per week. The unit is obtained by comparing an employee's average number of hours worked to the average number of hours of a full-time worker. Eurostat.

[1440] Question 34 from Business Survey and Question 28 from Stakeholder Survey. For the full results please see the Annex.

Figure 8.13: Expected social impacts for Option 3



Q34 Business Survey; 107 responses – Q28 Stakeholder Survey; 148 responses.

<u>Work conditions and labour rights</u>

The potential impacts on working conditions in the EU and non-EU countries as well as labour rights depend, on the one hand, on the extent to which social issues will be included and detailed in the reporting requirements, and, on the other hand, to the extent that mere reporting requirements are able to enact changes in companies' policies.

It can be expected that, similar to the previous option 2, the more issues related to employment and working conditions are expected to be included in company's reports, and the higher the likelihood of consequences for a failure to report, the higher is the likelihood that companies will report comprehensively on these issues. This may lead them to a more thorough consideration within companies of the underlying problems and risks and can increase the likelihood that actions are taken despite the fact that the regulation only requires reporting.

For example, the EU Non-Financial Reporting Directive (NFRD) requires reporting on companies' policies related to social responsibility and treatment of employees[1441], which can include a description of employee related policies such as retention, compensation, training and promotion. In the Impact Assessment[1442] of the NFRD it is argued that this increased transparency on employee- and human capital matters could potentially improve employment relations, and that it could enhance the equality of treatment and opportunities for different groups of people (gender, age, nationality, background, etc.).

[1441] European Commission (n.d.). Non-financial reporting. Available at: https://ec.europa.eu/info/business-economy-euro/company-reporting-and-auditing/company-reporting/non-financial-reporting_en.
[1442] See *commission staff working document impact assessment* accompanying the document *proposal for a directive of the european parliament and of the council* amending Council Directives 78/660/EEC and 83/349/EEC as regards disclosure of non-financial and diversity information by certain large companies and groups. Available at https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52013SC0127.

The Impact Assessment also finds that affected companies would be encouraged to better identify potential risks relating to human rights, including labour rights.

The Alliance for Corporate Transparency project[1443] analyses the implementation of the EU NFRD by assessing how European companies disclose information on their sustainability impact. The purpose of this three-year research project is to analyse the corporate disclosure on sustainability issues by the 1000 largest companies operating in the EU. In their first report, the Alliance for Corporate Transparency assessed the reports of 105 European companies from the Energy, ICT and Health Care sectors in 2018. The results show that reporting by these companies varies significantly across companies. Regarding social, employee and human rights, the results show that although 54% of companies describe their policies in general, only 38% specify key issues and targets. Moreover, only 37% and 50%, respectively, of the companies describe their due diligence process and outcomes related to social, employee and human rights. In contrast, the risks seem to be described relatively well: 45% of companies described general risks and an additional 35% describe specific risks, while 55% included also risks related to business partners and supply chains. The authors conclude that although most companies at least present some non-financial information and acknowledge the importance of environmental and social issues, only for less than 40% of companies the information on social and anticorruption matters is "clear in terms of concrete issues, targets and principal risks".

Moreover, a survey[1444] conducted in 2016 among companies which were subject to the UK's enhanced non-financial reporting requirements showed that only 15% of the participating companies experienced a change in their business policies/approach to employee matters over the last two years, since the introduction of the EU NFRD into Member State law. Of these companies 44% attributed the changes to the non-financial reporting requirements. A small share of companies (7%) also indicated that they experienced a change in their business policies/approach to social and community matters, and the large majority (67%) attributed the changes to the reporting requirements. Although the share of companies which has seen a change in their policies in response to the reporting requirements remains small, it suggests that mere reporting requirements could be able to also induce a change in companies' policies.

In an Impact Assessment[1445] on the Australian Modern Slavery Reporting Regulation it is expected that the reporting requirements will have a positive impact on work conditions also in third countries, as the regulation is expected to reduce modern slavery risks in the supply chains of Australian goods and services. It is argued that the reporting requirements will set clear standards for action and will facilitate a 'race to the top' amongst business, which will make it more likely that companies comply with the due diligence requirements and that social impacts take place.

[1443] Alliance for Corporate Transparency Project (2019). 2018 Research Report. Available at: https://www.allianceforcorporatetransparency.org/.

[1444] The Impact of Non-Financial Reporting, IFF-Belmana survey interim results, commissioned by the Department for Energy and Industrial Strategy in 2016. Cited in: UK Government (2016). Impact Assessment (IA) NFRD, No: BISCFA001. Available at: https://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=1&cad=rja&uact=8&ved=2ahUKEwiR_-qdne_jAhVIIlAKHRi1BGcQFjAAegQIAhAC&url=https%3A%2F%2Fassets.publishing.service.gov.uk%2Fgovernment%2Fuploads%2Fsystem%2Fuploads%2Fattachment_data%2Ffile%2F575540%2FNFRD_impact-assessment-_final_August_2016.pdf&usg=AOvVaw2I0OypxJ-4sfx-veRd2bGP.

[1445] Australian Government, Department of the Prime Minister and Cabinet (2018). Modern Slavery Reporting Requirement. Available at: https://ris.pmc.gov.au/2018/07/18/modern-slavery-reporting-requirement.

Overall, it is expected that mandatory reporting requirements could have some impacts on working conditions as well as labour rights, if these issues are expected from company reports in the reporting requirements. However, this is based on the assumption that public reporting raises reputational costs for misbehaviour, and thereby increases pressure not only to *report* but to substantively improve the underlying practices about which companies are required to report. The reporting requirements could therefore encourage companies to better identify and address potential risks concerning work conditions (and labour rights) and incentivise them to improve these not only in the EU itself but also in third countries where legal requirements regulating social impacts are weak or weakly enforced.[1446]

However, it is also important to keep in mind that under a reporting requirement companies are merely required to report on their policies and activities, but that they are not legally required to take actions to improve work conditions in their supply chains. As a result, reporting requirements have a limited ability to influence changes in companies' actions and policies. Moreover, as set out in the Regulatory Review, reporting requirements usually do not impose sanctions on the failure to report or for reporting human rights violations, which usually leads to low levels of implementation.

Expected positive social impacts

Most of the business respondents to the survey[1447] expect positive impacts along their supply chains related to working conditions such as the elimination of discrimination in respect of employment and occupation (64%), the social dialogue (58%), as well as the quality of jobs (56%). Again, stakeholder views are relatively similar to those of the business respondents: Positive impacts are also expected by many stakeholders for the social dialogue (59%), for the quality of jobs (57%) and the freedom of association and effective recognition of the right to collective bargaining (55%).

However, many respondents also expect positive impacts on basic human and labour rights, the same as for option 2: 62% of business respondents and 65% of stakeholder respondents expect positive impacts on the effective abolition of child labour, while 59% of business respondents and 65% of stakeholder respondents expect positive impacts for the elimination of all forms of forced or compulsory labour.

[1446] University of Edinburgh (2010). Study of the Legal Framework on Human Rights and the Environment Applicable to European Enterprises Operating Outside the European Union. Available at: http://ec.europa.eu/enterprise/policies/sustainable-business/files/business-human-rights/101025_ec_study_final_report_en.pdf.
[1447] Again, it has to be pointed out that only those respondents who indicated that the option is likely to have social impacts or had no opinion were asked the more detailed question about which social impacts. Also, as stated before, it is important to keep in mind that respondents were surveyed on the basis of general questions without details about the elements of each option.

Table 8.50: Overview of the main areas of social impact where positive impacts are expected (Option 3)

Social Impact	Expectation of positive impact (rather than neutral or negative)	
	Business respondents	*General stakeholders*
Effective abolition of child labour	62%	65%
Elimination of all forms of forced or compulsory labour	59%	65%
Elimination of discrimination in respect of employment and occupation	64%	54%
Social dialogue	58%	59%
Quality of jobs	56%	57%
Freedom of association and effective recognition of the right to collective bargaining	49%	55%
Q35 Business Survey; 66 responses – Q29 Stakeholder Survey; 83 responses.		

Employment

Regarding the impact on employment, it can be argued that a mandatory reporting requirement could increase potentially the number of jobs related to CSR and compliance, if new mandatory reporting requirements would create more work. However, it is noted that the EU NFRD and other reporting requirements already exist, and that many companies are already expected to provide the required information in company reports. As such, the number of additional jobs which may be created as a result of a mandatory reporting requirement is expected to remain very limited. It is not expected that potential additional costs for a company due to the reporting requirements would be of an extent that this could lead to a considerable negative economic impact on companies and a resulting decrease in production jobs.

The results from the survey are mixed: Concerning the number of jobs, business respondents to the survey mostly expect a positive impact (40%, as opposed to a neutral impact (35%), negative impact (5%), or no opinion (21%)), whereas non-business stakeholders mostly expect (56%) a neutral impact (as opposed to a positive impact (18%), negative impact (5%) or no opinion (21%)).

Impact on Human Rights

The potential impacts of reporting requirements on human rights depend on not only the extent to which human rights will be included and detailed in the reporting requirements, but additionally on the ability to measure such rights as well as on their ability to enact changes in companies' policies. There is significant literature that speaks to the opportunities made available by establishing reporting requirements for companies to comply with their duties. For example, the EU Commission Impact Assessment on the EU NFRD Proposal (2013)[1448] found that introducing the requirement for companies to disclose material relating to social, human rights and anticorruption aspects as well as boards' diversity would have a beneficial impact on fundamental rights. Including such measures in the in the existing Accounting Directives would encourage EU companies to regularly review their policies and internal procedures in various aspects, mainly due to a larger public scrutiny. Not only can such reporting requirements be expected to have indirect positive impacts such as on the workers' right to information (Article 27 of the Charter of Fundamental Rights of the EU137) they can additionally be expected to have direct positive effects on companies' awareness of human rights. By specifically requiring companies to disclose risks in the field of human rights, reporting requirements can translate into a reduction EU company involvement in incidents of human rights violations. Disclosure of company policy relating to diversity and gender equality can lead to dialogue within the company and catalyse the promotion of the right to non-discrimination (Article 21 of the EU Charter) and the right to equality between women and men (Article 23). According to the Impact Assessment, such reporting requirements could even extend positive impacts to the freedom to choose an occupation and the right to engage in work (Article 15), as well as in the longer term on the freedom of expression and information (Article 11).

Benefits linked to increased awareness of human rights can go beyond the development of measures to protect fundamental rights within a firm. A potential indirect effect of human rights awareness – which are linked to reputational issues mentioned in Option 2 – is the increased concern for establishing partnerships up and downstream the supply chain with companies that share these concerns and build strategies to make their business models compatible with a human rights perspective.[1449] This potential benefit is consistent with the views presented in the interviews about current practices, in which respondents highlight the efforts that they have carried out to spread due diligence across their different units and how a comprehensive approach to due diligence may increase opportunities to work with partners that implement sustainable business-models.

However, as reporting requirement's impacts on human rights are dependent on their ability to enact changes in companies' policies, below we present the perceptions of companies and stakeholders regarding general and specific human rights impacts of the implementation of a new regulation requiring due diligence reporting.

[1448] See COMMISSION STAFF WORKING DOCUMENT IMPACT ASSESSMENT Accompanying the document Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL amending Council Directives 78/660/EEC and 83/349/EEC as regards disclosure of non-financial and diversity information by certain large companies and groups. Available at https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52013SC0127

[1449] Xu, L., Kumar, D.T., Shankar, K.M. et al. (2013). Analysing criteria and sub-criteria for the corporate social responsibility-based supplier selection using AHP. International Journal of Advanced Manufacturing Technology, 68(1-4), pages 907-916. https://doi.org/10.1007/s00170-013-4952-7

The effectiveness of reporting requirements in increasing protection for rights-holders is a frequently debated topic. While reporting requirements are frequently perceived to be procedural requirements which do not lead to substantive impacts, the majority of stakeholders foresee reporting requirements to have positive impacts for rights-holders regarding the right to freedom from slavery (67%) and non-discrimination/equality (64%). Accordingly linked, over 60% of respondents likewise expected such requirements to hold companies responsible to respect their human rights duties concerning women's rights, the rights of indigenous persons, and the rights of the child. Moreover, the majority of companies also indicated that new regulatory reporting requirements could have positive impacts on their supply chain regarding the rights of the child (68%), and the right to freedom from slavery (67%).

However, according to Source Intelligence (2014),[1450] companies' respect for their human rights duties is not necessarily affected by reporting requirements because companies already recognize that public opinion is overwhelmingly in favour of transparency in the responsible production of goods. As such, companies should be expected to voluntarily provide transparent reporting of their respect for human rights as a tool to gain consumer acceptance.

Thus, on one hand, companies are confident that reporting requirements will have positive human rights impacts, specifically on the rights of the child (68%) and the right to freedom from slavery (67%). It is noted that many business survey respondents would already be subject to the EU NFRD and other corporate reporting requirements in their Member States (which are discussed in the Regulatory Review). As such, reporting requirements can be foreseen to have a positive human rights impact mainly relating to those companies not already reporting, and only if compliance and transparency mechanisms are to be put in place and properly enforced.

A 2018 study by Alliance for Corporate Transparency[1451] assessed whether companies provided the type of information explicitly required by the Non-Financial Reporting Directive (NFRD), which includes sustainability, human rights, and environmental factors. The study found that over 90% of companies express in their reports a commitment to respect human rights and over 70% endeavour to ensure the protection of human rights even in their supply chains. This is in line with our survey responses where 46.6% of companies use direct human rights language to classify their due diligence practices and 70.85% of companies claim to have undertaken human rights due diligence. However, according to the 2018 study, a majority of companies they surveyed, do not provide any information that would allow a stakeholder to understand how this commitment is put into practice. Only 36% describe their human rights due diligence system, 26% provide a clear statement of salient issues and 10% describe examples or indicators to demonstrate effective management of those issues.

Similarly in the retail sector, a study by Deakin University and Queensland University of Technology investigated workplace human rights disclosure practices by 18 major Australian garment and retail companies that source products from developing nations.

[1450] Source Intelligence works to bring transparency and visibility to the supply chains of companies around the world. The goal is to provide an environment through platform technology where suppliers, partners, vendors, small businesses, and global brands have the ability to proactively address their compliance and transparency needs.

[1451] Alliance for Corporate Transparency Project, "2018 Research Project: The state of corporate sustainability disclosure under the EU Non-Financial Reporting Directive", at 6, available at: http://www.allianceforcorporatetransparency.org/assets/2018_Research_Report_Alliance_Corporate_Transparency-66d0af6a05f153119e7cffe6df2f11b094affe9aaf4b13ae14db04e395c54a84.pdf (last accessed on 5 March 2019).

The investigators found that the reviewed corporations only reported less than half of the specific disclosure categories, confirming that the lack of transparency enforcements in reporting requirements act as barriers to significant benefits for rights-holders.[1452]

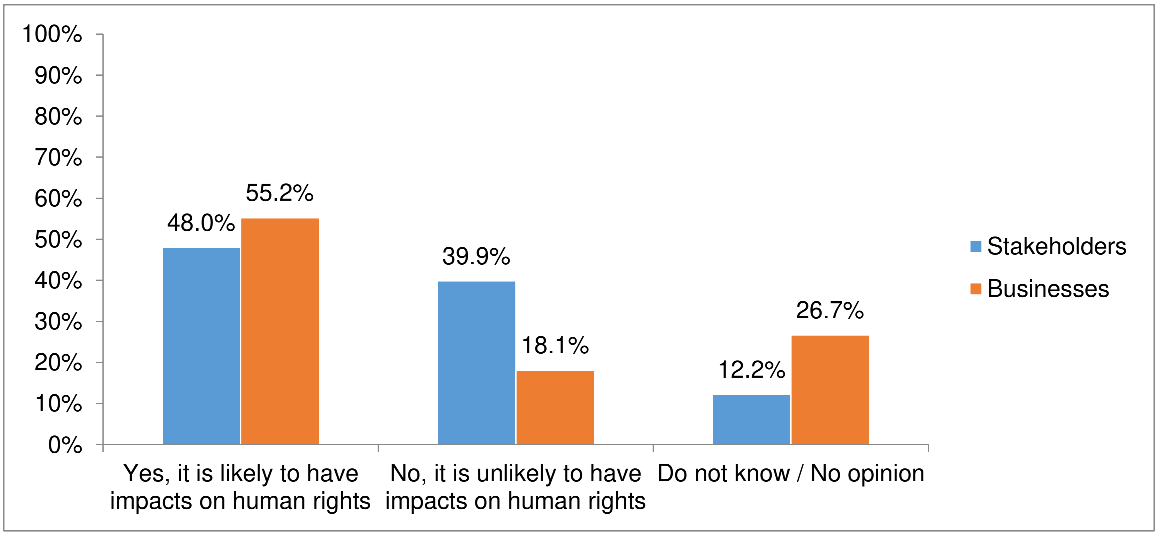
Interestingly, the areas where the majority of both stakeholders and companies expect neutral impacts are the right to privacy and the right to own property (42-47% respectively). The neutrality of these duties may be due to the slightly lower relevance of such rights in the work place relative to the rights of the child and the right to freedom from slavery, or the difficulties in ensuring the enjoyment of such rights via reporting requirements.

Finally, very few (0% to 5%) of respondents expect a negative impact, rather than a positive or neutral impact. The literature suggests that as reporting requirements might not have a significant impact on companies that already perceive the value of transparent reporting for their consumer base, impacts will focus most on those companies that do not willingly report.

<u>Expected human rights impacts</u>

When stakeholders and companies were asked whether the introduction of new regulatory reporting requirements for due diligence through the supply chain would have an impact on human rights, responses differed among the surveyed population. Almost half of all stakeholders and companies surveyed agreed that the introduction of such requirements is likely to have an impact on human rights, where stakeholders were slightly more skeptical about the impact (48%) than businesses (55.2%). The difference between both groups is starker when looking at those that do not foresee reporting requirements to have an impact on human rights, with 39.9% of stakeholders holding that perspective, versus 18.1% of companies, who were more likely to state no opinion (26.7%).

Figure 8.14: Expected human rights impacts under Option 3



Q38 Business Survey; 105 responses – Q32 Stakeholder Survey; 148 responses.

[1452] Azizul Islam, Muhammad, and Ameeta Jain. "Workplace human rights reporting: a study of Australian garment and retail companies." Australian accounting review 23, no. 2 (2013): 102-116. Retrieved from: https://onlinelibrary.wiley.com/doi/pdf/10.1111/auar.12009

Specific impacts by human rights areas

The majority of stakeholder respondents considered that new regulatory reporting requirements could have positive impacts regarding the right to freedom from slavery (67%) and to non-discrimination/equality (64%). Additionally, over 60% of respondents foresee positive impacts on women's rights, the rights of indigenous persons, and the rights of the child. The areas where most stakeholders expect neutral impacts are the right to privacy and to own property (46% respectively), and the right to freedom from arbitrary arrest (41%). Very few (0% to 2.5%) of respondents expect a negative rather than positive or neutral impact.

The majority of companies indicated that new regulatory reporting requirements could have positive impacts on their supply chain regarding the rights of the child (68%), and the right to freedom from slavery (67%). Over 60% of respondents expect positive impacts on the right to not be subject to torture and the right to life, liberty and security of person. Similar to stakeholder respondents, the areas where most companies foresee neutral impacts are the right to own property (47%) and the right to privacy (42%). Very few (0% to 5%) of respondents expect a negative impact, rather than a positive or neutral impact.

Table 8.51. Specific human rights impacts by area (Option 3)

	Stakeholders				Businesses			
	Negative	Neutral	Positive	No opinion / don't know	Negative	Neutral	Positive	No opinion / don't know
Right to Life, Liberty and Security of Person	0.00%	27.50%	53.75%	18.75%	1.49%	22.39%	59.70%	16.42%
Right to Physical / Mental Health	0.00%	26.58%	56.96%	16.46%	1.49%	25.37%	56.72%	16.42%
Right to not be subject to Torture	0.00%	35.44%	48.10%	16.46%	1.52%	21.21%	63.64%	13.64%
Right to Freedom of Opinion/Expression	2.53%	32.91%	48.10%	16.46%	4.55%	31.82%	50.00%	13.64%
Right to Non-Discrimination / Equality	1.28%	20.51%	64.10%	14.10%	4.62%	27.69%	56.92%	10.77%
Right to own Property	1.27%	45.57%	29.11%	24.05%	3.03%	46.97%	30.31%	19.70%
Right to freedom from Slavery	1.27%	17.72%	67.09%	13.92%	2.98%	19.40%	67.16%	10.45%
Right to Freedom from Arbitrary Arrest	1.28%	41.03%	32.05%	25.64%	2.99%	37.31%	40.30%	19.40%
Right to Privacy	0.00%	45.57%	34.18%	20.25%	1.52%	42.42%	37.88%	18.18%
Right to Peaceful Assembly / Association	0.00%	27.85%	54.43%	17.72%	1.52%	33.33%	54.55%	10.61%
Right to Education	1.27%	37.97%	43.03%	17.72%	1.52%	31.82%	51.51%	15.15%
Rights of the Child	0.00%	22.78%	62.03%	15.19%	1.52%	18.18%	68.18%	12.12%
Women's Rights	1.27%	21.52%	63.29%	13.92%	1.52%	25.76%	59.09%	13.64%
Rights of Indigenous Persons	1.27%	21.52%	63.29%	13.92%	3.03%	25.76%	53.03%	18.18%
Rights of People with Disabilities	0.00%	35.00%	48.75%	16.25%	2.94%	27.94%	50.00%	19.12%
Q33 Stakeholder Survey; 81 responses.					**Q39 Business Survey; 70 responses.**			

Environmental Impacts

The potential environmental impacts of reporting requirements depend on not only the extent to which they will be included and detailed in the reporting requirements, but additionally on the taxonomy used as well as on their ability to enact changes in companies' policies. There is significant literature that speaks to the opportunities made available by establishing reporting requirements for companies to act responsibly towards the environment. For example, the EU Commission Impact Assessment on the EU NFRD Proposal (2013)[1453] found that positive impacts on environmental awareness can be expected to increase via the improved transparency that reporting requirements provide and better quality of information on companies' environmental performance. This would have an indirect positive environmental impact by increasing peer pressure and raising reputational costs for misbehaviour, which would lead to improvements on businesses' conduct.

Complementing survey results with the interviewees' views about the inclusion of environmental and climate change in current due diligence practices, the results illustrate that due diligence based on reporting guidelines such as UNGP have potential positive effects on the internal and external scopes of action. On the internal level, improved knowledge of the company and the supply chain – due to increased transparency – may help overcome the silo mentality in businesses in which the different units within a firm do not share goals, tools priorities and processes. On the external level, interviews presented positive views indicating that as more firms adopted due diligence frameworks based on the environment and human rights, companies tended to find it easier to 'cross-paths' with other sustainable businesses.

Interviewees also noted that with the existing legal framework, a primary motivation to undertake these types of due diligence is exposure to public scrutiny. The views shared regarding due diligence practices in own operations indicate that there are neither sufficient resources nor systematic efforts dedicated to implement comprehensive programmes to prevent, mitigate or remedy potential environmental or human rights impacts. Taking this into account, the extent and scope of disclosure instructed by due diligence reporting requirement will indirectly condition businesses environmental performance based on the capacity of the regulation to prompt the systematic adoption of environmental and human rights due diligence.

Regarding these indirect positive effects, a study analysing the potential of the EUNFRD to stimulate organisational change indicated that the capacity of the Directive to induce ex-ante organisational learning and changing business conducts is weakened by its ex-post accountability focus, in which sanctions are applied to non-disclosure, not accuracy[1454]. In this sense, the authors recommend that reporting requirements clarify the importance of management-anchoring of reporting as learning opportunities to reduce internal and external risks. Additionally, emphasising the learning aspect of the reporting process should entail interaction between firms and stakeholders to build

[1453] See COMMISSION STAFF WORKING DOCUMENT IMPACT ASSESSMENT Accompanying the document Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL amending Council Directives 78/660/EEC and 83/349/EEC as regards disclosure of non-financial and diversity information by certain large companies and groups. Available at https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52013SC0127

[1454] Buhmann, K. (2018). Neglecting the proactive aspect of human rights due diligence? A critical appraisal of the EU's non-financial reporting directive as a Pillar One avenue for promoting Pillar Two Action. *Business and Human Rights Journal,* 3(1), pp. 23-45. Available at: https://doi.org/10.1017/bhj.2017.24

common frameworks that guide comprehensive due diligence processes to prevent harm.

Below, we present the perceptions of companies and stakeholders regarding general and specific environmental impacts of the implementation of a new regulation requiring due diligence reporting. Compared to the new voluntary guidelines, where most of the stakeholders declared that they did not expect any environmental impact, the new regulation requiring due diligence reporting shows a stronger level of agreement between companies and stakeholders on the likelihood of environmental impacts. However, there is also a higher level of uncertainty, as more respondents prefer not to give an opinion than in the previous option.

Like in Option 2, stakeholders and companies who foresee environmental effects identify similar areas that are likely to have positive impacts, the most relevant is environmental air pollution, followed by waste, and water resources. Areas where respondents show diverging expectations are energy use and mix, and transport. As in the results for Option 2, companies show more uncertainty regarding specific impacts, probably because some of them are beyond the scope of their business operations or unknown to the individual survey respondent. Additionally, this uncertainty is extended to stakeholders, who refrain from identifying the type of impact at a higher rate compared to the previous option.

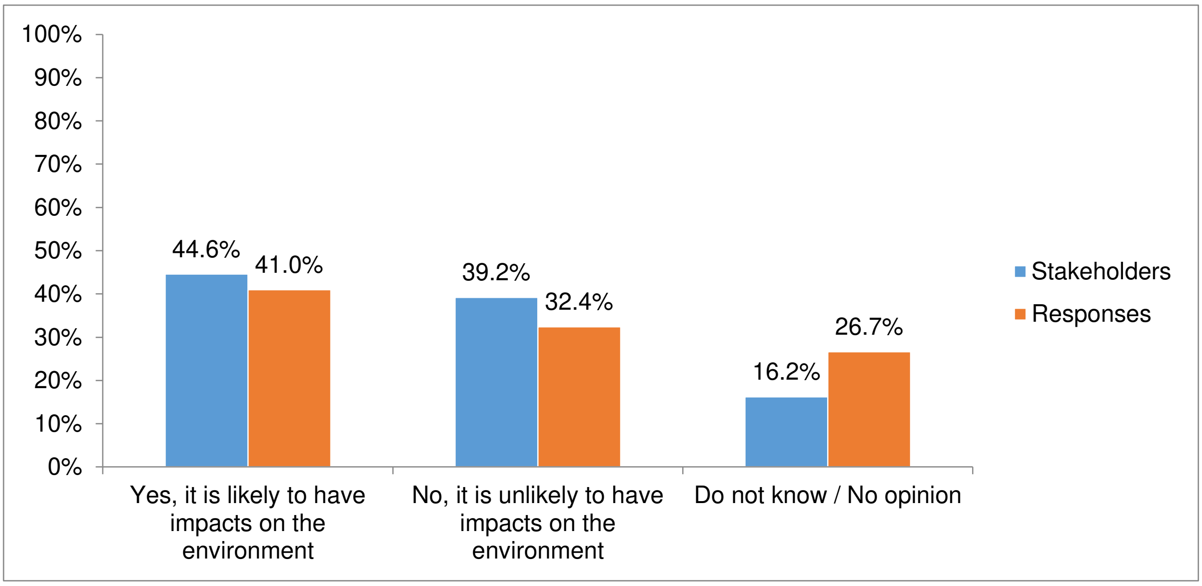
Generally, reporting requirements have low levels of enforcement, as they do not impose a sanction for non-compliance, nor do they provide for legal liability or access to remedy. These characteristics might be one source of uncertainty, particularly when respondents do not have information on how such regulation would be implemented.

With the current data, it is not possible to determine the specific concerns of companies; however, recent reporting instances serve as examples of the extent of disclosure that could be anticipated from corporate actors. For instance, the EU NFRD has two main risk perspectives to guide the process of reporting potential effects on the environment and climate change. On the one hand, the climate-related information should include the principal risks to the development, performance and position of the company resulting from climate change. On the other, companies should disclose the main risks of a negative impact on the climate resulting from the company’s activities. Along the same line, the new non-binding Guidelines on reporting climate-related information stress the critical role of companies and financial institutions in the transition to a climate-resilient economy. The Guidelines acknowledge the need for companies to better understand and address the risks of negative impacts on the climate resulting from their operation.

Expected environmental impact

Most stakeholders (45%) and companies (41%) declared that they expect that new regulation requiring due diligence reporting is likely to have an impact on the environment. However, there is a significant proportion of stakeholders that indicate the opposite (39%), whereas companies that do not expect environmental impacts are near 30%. Around 16% of stakeholders and 27% of companies are unable to tell whether requiring due diligence reporting is likely to have impacts, indicating a considerable level of uncertainty among both types of respondents.

Figure 8.15: Expected environmental impacts under Option 3



Q36 Business Survey; 105 responses – Q30 Stakeholder Survey; 148 responses.

<u>Specific impacts by environmental area</u>

Environmental air pollution and waste are the areas that most stakeholders (60%) and companies (63%) expect to receive positive impacts from new regulation requiring due diligence reporting. Areas with more than 50% of mentions by stakeholders and companies are water resources (51% and 62% respectively) and greening of the economy (51% and 56%). The areas where stakeholders and companies have diverging expectations regarding positive impacts are energy use and mix (49% versus 62%) and transport (42% versus 52%). Uncertainty regarding the impacts on different areas is higher among companies that in stakeholders, near 30% of companies declare that they do not know or have no opinion on potential impacts in 4 out of 10 areas, and near 25% of stakeholders declare that they do not have an opinion in all areas.

Table 8.52: Specific impacts by environmental area (Option 3)

	Stakeholders				Businesses			
	Negative	Neutral	Positive	No opinion / don't know	Negative	Neutral	Positive	No opinion/don't know
Environmental Air Pollution	0.0%	16.7%	60.3%	23.1%	1.9%	18.5%	63.0%	16.7%
Waste	0.0%	16.7%	59.0%	24.4%	1.9%	14.8%	64.8%	18.5%
Energy use and mix	0.0%	24.4%	48.7%	26.9%	1.9%	21.2%	61.5%	15.4%
Transport	0.0%	29.5%	42.3%	28.2%	3.7%	27.8%	51.9%	16.7%
Water Resources	0.0%	23.1%	51.3%	25.6%	3.8%	15.1%	62.3%	18.9%
Biodiversity	0.0%	28.2%	46.2%	25.6%	1.9%	22.6%	45.3%	30.2%
Agricultural Fertilisers	1.3%	19.2%	53.9%	25.6%	3.8%	20.8%	47.2%	28.3%
Forests	1.3%	24.4%	50.0%	24.4%	5.7%	17.0%	47.2%	30.2%
Fisheries	2.6%	29.5%	39.8%	28.2%	1.9%	20.8%	43.4%	34.0%
Greening of the Economy	1.3%	17.7%	50.6%	30.4%	3.6%	18.2%	56.4%	21.8%
Q31 Stakeholder Survey; 79 responses.					**Q37 Business Survey; 56 responses.**			

Impacts on Public Authorities

Similar to Option 2, this option would most likely entail costs for an external study to define the exact reporting requirements and draft guidelines on the implementation of the reporting as well as promotion activities. In addition, this option may entail personnel costs for staff at the EC providing guidance on the implementation, and depending on the legal oversight required at EU level, may include conducting sample reviews of due diligence reports. In the Impact Assessment regarding the Conflict Minerals Regulation the costs for implementing guidance for voluntary to mandatory regulatory options range from 1.5 to 2 FTEs. Again, it is noted that the scope of the Conflict Mineral Regulation is limited to a certain sector and that a more general due diligence requirement which applies to a larger set of companies would imply larger costs.

Depending on the design of the new regulation, it may also be foreseen to create a database either on Member State or EU-level to make relevant company reports easily accessible to the public. This could create additional costs related to the set-up and maintenance of this database, e.g. ongoing costs related to the collection of reports and regular updating of the database. The financial implications estimated for the Australian Modern Slavery Bill 2018[1455] include the establishment of an Anti-Slavery Business Engagement Unit (BEU) which shall provide expert support and advice to business on modern slavery risks and manage a central repository of modern slavery statements. The cost for this is estimated at approximately 550,000 EUR[1456] per year, which is expected to allow for 5 employees (FTEs) which are responsible for 3,000 reporting entities. The comparability of these cost estimates would largely depend on the number of companies to which the new regulation would apply and the level of detail which would be required in reports.

If an ex post study to assess the implementation and its effects may be required, this would pose an additional estimated cost of 200,000-300,000 EUR. Reporting requirements on non-financial matters do not usually imply access to judicial remedies for external stakeholders in the case of failure to report, and therefore there are no additional costs expected for the judicial system. At Member State level, reporting requirements could lead to legal remedies for shareholders or regulatory sanctions in terms of ordinary corporate law. It is assumed that these will be enforced in the usual way and would not lead to additional costs for the state. However, this depends on the potential design of the new regulation and its implementation at Member State level.

[1455] Parliament of Australia, Department of Parliamentary Services (2018). Modern Slavery Bill 2018. BILLS DIGEST NO. 12, 2018–19. Retrieved from: https://parlinfo.aph.gov.au/parlInfo/search/display/display.w3p;query=Id%3A%22legislation%2Fbillsdgs%2F6150516%22

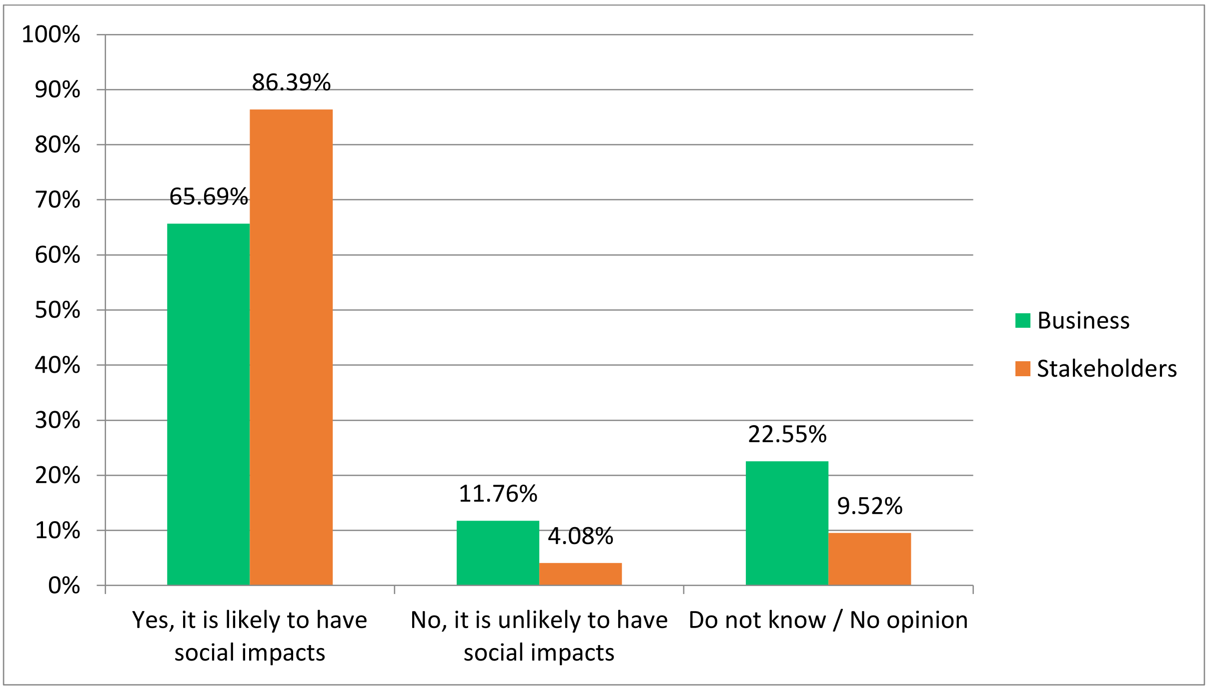
[1456] The Australian Government allocated 3.6 million Australian Dollars over four years in the 2018-19 Budget for the establishment of an Anti-Slavery Business Engagement Unit (BEU).

- **Option 4: New regulation requiring mandatory due diligence as a legal duty o care**

Social impacts

A large majority of business and stakeholder respondents expects social impacts from a new regulation requiring mandatory due diligence:[1457] 86% of stakeholder respondents and 66% of the business respondents think that there would be a social impact from mandatory due diligence. Only 4% of stakeholders and 12% % of the business respondents do not expect any social impacts from this regulatory option. Looking at specific sub-groups of stakeholders, 52% of respondents from civil society/NGOs and 18% of respondents from industry organisations expected social impacts. Again, a large share of respondents did not provide any response (44% and 68%, respectively).

Figure 8.16: Expected social impacts under Option 4



Q45 Business Survey; 102 responses – Q38 Stakeholder Survey; 147 responses.

<u>Work conditions and labour rights</u>

It is likely that social impacts will be highest if mandatory due diligence requirements are introduced. As set out in the Regulatory Options, a mandatory regulation on due diligence would require a company to identify and assess ongoing and potential impacts, act upon the findings, assess the effectiveness of the actions taken and report on these. For example, the French Vigilance Law requires companies to develop and implement a due diligence plan[1458] and to identify and prevent human rights violations and environmental damages in connection with their operations, which includes actions to

[1457] Q45 in the Business Survey and Q38 in the Stakeholder Survey. For the full survey results, please see the Annex.
[1458] "The plan shall include the reasonable vigilance measures to allow for risk identification and for the prevention of severe violations of human rights and fundamental freedoms, serious bodily injury or environmental damage or health risks resulting directly or indirectly from the operations of the company and of the companies it controls within." Source: European Coalition of Corporate Justice (2016). French Corporate Duty of Vigilance Law (English Translation). Available at: http://www.respect.international/french-corporate-duty-of-vigilance-law-english-translation/.

mitigate identified risks and mechanisms to assess measures that have been implemented. The law covers due diligence measures to identify risks and prevent "violations of human rights and fundamental freedoms, serious bodily injury or environmental damage or health risks". As the French law has only been adopted in 2017, and litigation in terms of the Act has not yet been brought, it is too early for any comprehensive assessments of its implementation and effects. The non-profit organisation Shift has issued a first report[1459] on human rights reporting in France, which aims to assess in how far the French legislation has a positive impact on the reporting activities. However, for the moment only the baseline report exists and the second report assessing possible improvements as a result of the legislation has not yet been issued.

Therefore, for the moment only anecdotal evidence can be assessed. One example of a CSR report[1460] describes measures taken under the French Vigilance Law in three main areas: integrity and employee engagement, safety and environmental stewardship. The report lists measures related to the learning, pay policy and inclusion policy, gender equality, employee relationship, and their safety measures. Such measures could improve the working conditions of workers within the company, its subsidiaries and the companies which it controls. However, it is not known whether these measures were really taken in response to the Vigilance Law.

Under this option the social impacts also depend to a large extent on how the regulation is implemented and enforced. Labour rights and working conditions are already regulated at both national and international level, but, as discussed in the Problem Analysis, enforcement is problematic, particularly in supply chains and third countries. Insofar as mandatory due diligence regulation would add a legally binding dimension to these existing expectations, it is likely to increase the practical uptake of those existing standards, thereby improving the labour conditions in question.

Social impacts in third countries

Social impacts in third countries arising from a new mandatory due diligence also depend on the scope of operations and business relationships which a company has in the third country. It can be expected that mandatory due diligence requirements can lead to a positive impact on labour rights in third countries since multinational companies affected by the regulation would have global operations and value chains. These companies would not only be required to identify and assess potential adverse impacts but would also be obliged to comply with a certain standard of care in acting upon their findings and monitoring their actions. Therefore, it can be expected that due diligence by EU companies in their supply chains would support also a better compliance of the companies in its supply chain with labour standards, for example if EU companies would have codes of conduct for 1st tier suppliers and execute audits. Such requirements from EU companies could also make it easier for the host countries of the supply chain companies to implement labour standards in practice and thus support creating a level-playing in the host country of the supply chain company.

[1459] Shift (2018). Human Rights Reporting in France: A Baseline for Assessing the Impact of the Duty of Vigilance Law. Available at: https://www.shiftproject.org/resources/publications/loi-vigilance/.
[1460] XPO Logistics (2018). Corporate Social Responsibility Report. Available at: https://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=5&ved=2ahUKEwj0iLCu9-PjAhVHz6YKHUCNATAQFjAEegQIBBAC&url=https%3A%2F%2Fxpodotcom.azureedge.net%2Fxpo%2Ffiles%2FXPO_Logistics_2018_CSR_Report.pdf&usg=AOvVaw0n6qH-A-N-V50SRsiZk9TL.

However, it could also be possible that companies only do the minimum, depending on how the regulation is formulated. In this case they might just, for example, remove child labourers, but would not necessarily take broader measures and take care of remediation of negative impacts which they may have already caused. Another negative impact could be that some European companies withdraw from (developing) third countries where e.g. labour laws are infringed rather than addressing these issues, although this is not the aim of the regulation. This might have negative employment effects for the affected countries, and/or it could potentially lead to other companies from countries with no or less restrictive regulations entering these markets, which would have adverse impacts on the workers and working conditions in these countries. In practice, however, it is unlikely that companies would be in a position to restructure their global business model in such a significant way for this purpose. Similarly, the literature has also shown that companies very rarely terminate their business relationships (which includes exiting certain jurisdictions) based exclusively on social or human rights-related concerns.[1461]

Expected positive social impacts

Business and stakeholder respondents have largely the same expectations as for options 2 and 3 regarding the areas in which to expect positive social impacts. Again, business and stakeholder respondents mainly expect positive impacts on labour rights, i.e. the elimination of all forms of forced or compulsory labour (78% and 85%, respectively), and the effective abolition of child labour (77% and 85%, respectively). [1462]

The other areas where they largely expect positive social impacts are: the elimination of discrimination in respect of employment and occupation (74% of business respondents and 79% of stakeholders), the quality of jobs (67% of business respondents), wages (78% of stakeholders) and the freedom of association and effective recognition of the right to collective bargaining (67% of business respondents and 83% of non-business-respondents). Although these were also largely the areas where positive social impacts were expected for options 2 and 3, the share of respondents expecting positive impacts (rather than negative or neutral impacts) is higher for option 4. Very few respondents indicated that they expect negative social impacts.

Table 8.53: Overview of the main areas of social impact where positive impacts are expected (Option 4)

Social Impact	**Expectation of positive impact** **(rather than neutral or negative)**	
	Business respondents	***General stakeholders***

[1461] McCorquodale, R., Smit, L., Neely, S., & Brooks, R. (2017). Human Rights Due Diligence in Law and Practice: Good Practices and Challenges for Business Enterprises. Business and Human Rights Journal, 2(2), 195-224. doi:10.1017/bhj.2017.2. Available at: https://www.cambridge.org/core/journals/business-and-human-rights-journal/article/human-rights-due-diligence-in-law-and-practice-good-practices-and-challenges-for-business-enterprises/0306945323DD6F6C9392C5DBDE167001

[1462] Again, it has to be pointed out that only those respondents who indicated that the option is likely to have social impacts or had no opinion were asked the more detailed question about which social impacts. Also, as stated before, it is important to keep in mind that respondents were surveyed on the basis of general questions without details about the elements of each option.

Effective abolition of child labour	77%	85%
Elimination of all forms of forced or compulsory labour	78%	85%
Elimination of discrimination in respect of employment and occupation	74%	79%
Quality of jobs	67%	78%
Wages	61%	78%
Freedom of association and effective recognition of the right to collective bargaining	67%	83%
Q46 Business Survey; 74 responses – Q39 Stakeholder Survey; 130 responses.		

Employment levels

On the one hand, a new regulation could have negative impacts on employment levels if affected EU companies would become less competitive vis-à-vis competing companies from third countries with less restrictive due diligence requirements due to the increased economic burden from new mandatory due diligence requirements. This could especially be the case in the short run when companies would face increased cost from adapting and re-organising their supply chains while not yet benefiting from positive reputational effects as described below. If such an economic burden would lead to companies reducing their production, this would also have a negative impact on employment levels. Since option 4 is the most ambitious option, it is also the option where negative impacts on employment levels could take place most likely. However, this depends on how large the economic burden would be for each company as discussed above in the section on economic impacts.

On the other hand, there could also be positive impacts on employment levels within and outside of the EU, especially in the long run. First, there could be additional jobs created related to the new due diligence policies since the implementation of company policies regarding work conditions or labour rights might require more staff and staff with specialised expertise. The number of additional jobs created is expected to be higher than under option 3, as under this option companies do not only need to report on their activities, but they also need to have a comprehensive assessment of their supply chains and need to implement measures to address potential problems. Concrete numbers for employment effects were only possible to be calculated for large companies and are described under option 4.2(a), which is applicable to large companies only. However, these effects are expected to take place also for all other options which would apply to large companies, i.e. 4.1 for large companies in specific sectors, all sub-options of 4.2 and also sub-options 4.3.

Second, a new regulation could have a positive impact on employment levels if due diligence activities increase the reputation of a company and as a result increase the demand for its products as well as its competitiveness vis-à-vis companies from countries with less strict due diligence requirements. As a result of the latter two, these companies could increase their production and therefore their demand for labour. This could especially be the case for companies which are seen as frontrunners in regard to their due diligence activities and which manage to communicate their achievements well as they would benefit most from reputational effects.

The survey results indicate that respondents mostly expect positive or neutral impacts on employment levels from option 4. However, it is important to point out that the survey question did not specify whether the potential impacts were expected in the short or long term. Overall, most respondents expect positive impacts on the number of jobs (40% of business respondents and 45% of stakeholders), but there is also a large number which expects neutral impacts on the number of jobs (37% of business respondents and 34% of stakeholders). Only a very small share (4% of each group) expects negative impacts on the number of jobs, while 19% and 17% of business and stakeholder respondents, respectively, have no opinion.

Sub-option 4.1: Narrow category of businesses (limited by sector)

The social impacts of this sub-option depend, on the one hand, on the general factors described for option 4, i.e. on the scope and implementation of the new regulation. On the other hand, the social impacts of this option depend on the choice of sectors to which the regulation will be applicable. It can be assumed that social impacts would be higher if the regulations would cover sectors in which work conditions are considered to be relatively bad and in which labour rights tend to be enforced less well, or sectors which source heavily in countries which are known for bad work conditions and labour markets where labour rights do not exist or are not enforced. In order to assess which sectoral coverage would provide most social benefits an in-depth study would be necessary. One indicator for high-risk sectors where it could be expected that social impacts may be high are the OECD's sector-specific guidelines which accompany the general Due Diligence Guidance for Responsible Business Conduct. The OECD provides sector-specific due diligence for the following sectors: Minerals and mineral supply chains, garment and footwear, agriculture, extractives, financial sector.[1463] Another indicator could be a large study by the European Foundation for the Improvement of Living and Working Conditions[1464] which assessed working conditions and job quality in different European sectors. It concludes that European sectors vary considerably in terms to the work conditions. Sectors which, according to the report, score relatively poorly on the four considered indicators (earnings, prospects, intrinsic job quality and working time quality) are: administrative services, the agro-food industry, food and beverage services, textiles and clothing, transport and storage, and construction.

Concerning impacts on employment, the same considerations as discussed generally for option 4 apply. Depending on the sectoral coverage of a new regulation and whether the covered sectors employ more or less workers, the positive as well as negative impacts on employment could be stronger. For such considerations the table below shows the number of people employed in each industry sector in the EU. The two sectors in the EU

[1463] OECD (2018). OECD Due Diligence Guidance for Responsible Business Conduct. Available at: https://www.oecd.org/investment/due-diligence-guidance-for-responsible-business-conduct.htm.
[1464] European Foundation for the Improvement of Living and Working Conditions (2014). Working conditions and job quality: Comparing sectors in Europe. Available at: https://www.eurofound.europa.eu/publications/report/2014/working-conditions/working-conditions-and-job-quality-comparing-sectors-in-europe-overview-report

which employ most workers are wholesale and retail trade; repair of motor vehicles and motorcycles (15% of total employment) as well as manufacturing (14%).

Table 8.54: Overview of total employment in the EU by sector (in thousand persons)

Sector	2015	Share
Agriculture, forestry and fishing	10,874.79	5%
Mining and quarrying	670.09	0%
Manufacturing	31,652.76	14%
Electricity, gas, steam and air conditioning supply	1,247.95	1%
Water supply; sewerage, waste management and remediation activities	1,664.02	1%
Construction	14,544.00	7%
Wholesale/retail trade; repair of motor vehicles/ motorcycles	33,645.66	15%
Transportation and storage	11,398.58	5%
Accommodation and food service activities	11,367.91	5%
Information and communication	6,670.32	3%
Financial and insurance activities	5,979.23	3%
Real estate activities	2,537.86	1%
Professional, scientific and technical activities	14,099.69	6%
Administrative and support service activities	14,562.23	7%
Public administration/ defence; compulsory social security	14,631.87	7%
Education	15,584.17	7%
Human health and social work activities	24,125.44	11%
Arts, entertainment and recreation	4,062.78	2%
Activities of households as employers; undifferentiated goods- and services-producing activities of households for own use	3,700.99	2%

Source: Eurostat, Total employment domestic concept

Sub-option 4.2: Horizontally across sectors

Social impacts for these options are expected to be those as generally discussed under option 4. In addition, the level of expected social impacts of the different sub-options of 4.2 depend on the coverage of affected companies as described below.

Sub-option 4.2(a): Set of large companies

The social impacts of this sub-option depend on the number of companies to which the new regulation would apply. Given that 99% of EU companies are SMEs (enterprises employing less than 250 people)[1465], it can be expected that this sub-option would only apply to 1% of EU companies. However, this would depend on the definition of large companies and/or the definition of the affected group of companies. It is also noted that a significant number of these SMES are within the supply chains or value chains of the 1% of large companies. Insofar as the regulation would extend to due diligence through the supply chain, the standard of care required would indirectly apply to the practices of these SMEs through the large companies with which they do business.

It is assumed that this sub-option may lead to less social impacts than under sub-option 4.2(b) which covers the entire EU economy. Depending on the potential sectoral scope under option 4.1, the expected social impacts of this sub-option could be roughly similar as those expected under option 4.1 if the number of companies operating in the selected sectors is small. Both options do not apply to the entirety of companies but a sub-set of companies only.

We provide estimates for potential direct employment effects resulting from the implementation of a new regulation requiring due diligence measures by large companies. In order to calculate possible direct employment effects, annual cost estimates from the firm-level economic impact assessment (see section on economic impacts) were applied to calculate annual full-time equivalents (FTEs), i.e. the number of additional jobs, which could be created under this option. The estimates are presented in Table 8.55 below.

For the EU28, a new regulation requiring mandatory due diligence that would be applied to only large companies with more than 250 employees could create about 10,000 jobs. By comparison, a new regulation requiring new reporting requirements which would be applied to only large companies with more than 250 employees could create about 759 jobs. If mandatory DD would be applied horizontally across sectors for all businesses incl. SMEs, this regulation could create about more than 600,000 additional jobs in the EU.

It should be noted that these estimates are based on the person-days per due diligence activity which were indicated by the survey respondents. These estimates were applied to calculate the additional annual cost impacts for firms based in the EU. It should noted that these number have some limitations, which are outlined in the Section on firm-level economic impacts. Accordingly, the estimated employment effects should be interpreted with caution.

[1465] Eurostat (2018). Statistics on small and medium-sized enterprises. Available at: https://ec.europa.eu/eurostat/statistics-explained/index.php/Statistics_on_small_and_medium-sized_enterprises.

It should also be noted that there are likely to be countervailing effects, which can impact on the net impact on employment: It can be assumed that not all companies would hire new staff, but some companies would rather train existing staff (e.g. staff set free from rationalisation measures). In addition, due to rising labour costs, some companies may have to raise prices. Others, mainly smaller companies among the group of (Eurostat-defined) large companies and companies with small profit margins, may face profitability problems and may be driven out of business, which would reduce the net impact of such a new regulation on overall employment. Those companies that have to raise prices may face lower demand for their products and services, with adverse effects on employment. And finally, companies may find it difficult to hire qualified personnel, which moderates the total employment effect at least over the short- to medium-term.

Table 8.55: Potential employment effects, EU28

Policy option / company size	Additional annual firm-level cost, EU aggregate	Cost of one person-day (8 hrs)	Cost of one person-month (20 man-days)	Cost of one full time equivalent (FTE)	Number of FTEs derived from empirical estimates based on sum of man-days for individual activities
New reporting requirements					
SMEs	EUR 3,418,391,110	EUR 219.20	EUR 4,384.00	EUR 52,608.00	**64,979**
Large companies	EUR 39,935,855	EUR 219.20	EUR 4,384.00	EUR 52,608.00	**759**
	TOTAL				**65,738**
Mandatory DD throughout value chains					
SMEs	EUR 32,498,788,721	EUR 219.20	EUR 4,384.00	EUR 52,608.00	**617,754**
Large companies	EUR 543,451,881	EUR 219.20	EUR 4,384.00	EUR 52,608.00	**10,330**
	TOTAL				**628,084**

Source: Own calculations based on business stakeholder survey and Eurostat data.

Table 8.56: Potential employment effects resulting for new mandatory DD throughout companies' value chains, if applied only to large EU companies (>250 employees)

Country	Mandatory DD throughout value chains Empirical monthly labour estimates based on sum of person-days for individual activities	Mandatory DD throughout value chains Empirical monthly labour cost estimates based on total person-day estimates	Labour costs per hour	Cost of one person-day (8 hrs)	Cost of one person-month (20 person-days)	Cost of one full time equivalent (FTE)	Number of FTEs derived from empirical estimates based on sum of person-days for individual activities	Number of FTEs derived from empirical estimates based on total person-day estimates
EU28	EUR 2,696,608,264	EUR 4,148,628,098	EUR 27.40	EUR 219.20	EUR 4,384.00	EUR 52,608.00	**615,102**	**946,311**
Austria	EUR 79,535,248	EUR 122,361,920	EUR 34.00	EUR 272.00	EUR 5,440.00	EUR 65,280.00	**14,620**	**22,493**
Belgium	EUR 75,138,761	EUR 115,598,094	EUR 39.70	EUR 317.60	EUR 6,352.00	EUR 76,224.00	**11,829**	**18,199**
Bulgaria	EUR 7,047,734	EUR 10,842,668	EUR 5.40	EUR 43.20	EUR 864.00	EUR 10,368.00	**8,157**	**12,549**
Croatia	EUR 8,908,962	EUR 13,706,096	EUR 10.90	EUR 87.20	EUR 1,744.00	EUR 20,928.00	**5,108**	**7,859**
Cyprus	EUR 2,438,350	EUR 3,751,307	EUR 16.30	EUR 130.40	EUR 2,608.00	EUR 31,296.00	**935**	**1,438**
Czechia	EUR 42,040,555	EUR 64,677,777	EUR 12.60	EUR 100.80	EUR 2,016.00	EUR 24,192.00	**20,853**	**32,082**

Denmark	EUR 60,828,660	EUR 93,582,554	EUR 43.50	EUR 348.00	EUR 6,960.00	EUR 83,520.00	**8,740**	**13,446**
Estonia	EUR 4,462,611	EUR 6,865,556	EUR 12.40	EUR 99.20	EUR 1,984.00	EUR 23,808.00	**2,249**	**3,460**
Finland	EUR 42,541,363	EUR 65,448,251	EUR 33.60	EUR 268.80	EUR 5,376.00	EUR 64,512.00	**7,913**	**12,174**
France	EUR 317,287,667	EUR 488,134,873	EUR 35.80	EUR 286.40	EUR 5,728.00	EUR 68,736.00	**55,392**	**85,219**
Germany	EUR 870,073,467	EUR 1,338,574,565	EUR 34.60	EUR 276.80	EUR 5,536.00	EUR 66,432.00	**157,166**	**241,795**
Greece	EUR 13,682,682	EUR 21,050,279	EUR 16.10	EUR 128.80	EUR 2,576.00	EUR 30,912.00	**5,312**	**8,172**
Hungary	EUR 16,754,304	EUR 25,775,852	EUR 9.20	EUR 73.60	EUR 1,472.00	EUR 17,664.00	**11,382**	**17,511**
Ireland	EUR 31,247,167	EUR 48,072,565	EUR 32.10	EUR 256.80	EUR 5,136.00	EUR 61,632.00	**6,084**	**9,360**
Italy	EUR 190,504,762	EUR 293,084,249	EUR 28.20	EUR 225.60	EUR 4,512.00	EUR 54,144.00	**42,222**	**64,957**
Latvia	EUR 3,931,668	EUR 6,048,720	EUR 9.30	EUR 74.40	EUR 1,488.00	EUR 17,856.00	**2,642**	**4,065**

Lithuania	EUR 6,595,056	EUR 10,146,240	EUR 9.00	EUR 72.00	EUR 1,440.00	EUR 17,280.00	**4,580**	**7,046**
Luxembourg	EUR 13,379,162	EUR 20,583,326	EUR 40.60	EUR 324.80	EUR 6,496.00	EUR 77,952.00	**2,060**	**3,169**
Malta	EUR 478,911	EUR 736,786	EUR 14.70	EUR 117.60	EUR 2,352.00	EUR 28,224.00	**204**	**313**
Netherlands	EUR 123,440,283	EUR 189,908,128	EUR 35.90	EUR 287.20	EUR 5,744.00	EUR 68,928.00	**21,490**	**33,062**
Poland	EUR 70,660,974	EUR 108,709,190	EUR 10.10	EUR 80.80	EUR 1,616.00	EUR 19,392.00	**43,726**	**67,271**
Portugal	EUR 24,043,554	EUR 36,990,082	EUR 14.20	EUR 113.60	EUR 2,272.00	EUR 27,264.00	**10,583**	**16,281**
Romania	EUR 23,337,219	EUR 35,903,414	EUR 6.80	EUR 54.40	EUR 1,088.00	EUR 13,056.00	**21,450**	**32,999**
Slovakia	EUR 13,454,608	EUR 20,699,397	EUR 11.60	EUR 92.80	EUR 1,856.00	EUR 22,272.00	**7,249**	**11,153**
Slovenia	EUR 8,554,494	EUR 13,160,761	EUR 18.10	EUR 144.80	EUR 2,896.00	EUR 34,752.00	**2,954**	**4,544**
Spain	EUR 143,361,168	EUR 220,555,643	EUR 21.40	EUR 171.20	EUR 3,424.00	EUR 41,088.00	**41,870**	**64,415**

Sweden	EUR 80,380,334	EUR 123,662,053	EUR 36.60	EUR 292.80	EUR 5,856.00	EUR 70,272.00	**13,726**	**21,117**
United Kingdom	EUR 363,488,181	EUR 559,212,586	EUR 27.40	EUR 219.20	EUR 4,384.00	EUR 52,608.00	**82,912**	**127,558**

Sub-option 4.2(b): All business, including SMEs

The social impacts of this sub-option would be the same as those described in the general part under option 4, which describes an economy-wide application. It can be expected that the social impacts would be the highest if a new regulation requires mandatory due diligence which applies to all companies. However, as stated above, the social impacts depend to a large extent on how the new regulation is implemented. Labour rights or employee-related issues are already regulated to a large extend within the EU and its Member States, but a binding duty may influence and improve the implementation of these standards in practice.

Similarly, it can be expected that impacts (positive and negative) on EU employment levels – as described under option 4 – would be most be significant under this option given that the requirements would apply to all companies in the EU. The same is expected for social impacts in third countries.

Sub-option 4.2(c): All business plus specific additional obligations only applying to large companies

In addition to the social impacts expected for option 4.2(b), which are also generally described under option 4, this sub-option would require specific requirements for large companies. These could increase the social impacts compared to the previous options 4.1, 4.2(a) and 4.2(b). Where these additional social impacts would be expected, depends on the areas for which additional obligations would be specified. If these obligations would be specified in relation to environmental and climate change matters such as in the Paris Agreement, no additional positive impacts would be expected for work conditions, labour rights or other social matters. Concerning impacts on employment levels, the same considerations as under option 4 apply, i.e. if such additional obligations for large companies would constitute a significant economic burden, there may be negative impacts on employment to be expected. However, given the small share of large companies in the EU economy, this effect is expected to remain small. As discussed under option 4, potentially positive effects for employment could be created if improved due diligence regarding environmental and climate matters leads to better reputation and thus increased sales and production. In addition, a small number of new jobs may be created within these large companies for the purposes of climate change due diligence, which is a new and developing area.

Sub-option 4.3: Sub-options 1 and 2 accompanied by a statutory oversight and / or enforcement mechanism

It is noted that for a regulation to be "mandatory" it would need to be accompanied by some form of legal consequence for non-compliance, whether state-based oversight and / or judicial or non-judicial remedies. As such, one of the sub-options in sub-option 4.3 would always accompany sub-options 1 and 2.

The same considerations regarding social impacts apply to this sub-option as for the broad option 4.2(b) and those discussed generally under 4. It is expected that additional enforcement mechanisms foreseen under this sub-option would not increase the level of potential social impacts as such, since the due diligence requirements themselves would remain the same. However, if the enforcement mechanism increases compliance with the requirements, it will increase the likelihood that the expected social impacts come into effect.

Sub-option 4.3(a): Mechanisms for judicial or non-judicial remedies

As stated above under 4.3, the same considerations regarding social impacts apply to this sub-option as for the broad option 4.2(b) and those discussed generally under 4. In addition, it can be assumed that compliance would increase under this option and therefore it is more likely that the expected social impacts materialise. Social impacts could increase if the mechanism for remedies allows for remedies which improve social issues such as improving work conditions or improving labour laws. In the case that such remedies would pose a very high economic burden[1466] for companies, in theory this could have a negative impact on employment levels.

Sub-option 4.3(b): State-based oversight body and sanction for non-compliance

Similar to sub-option 4.3 (a), the same considerations regarding social impacts apply to this sub-option as for the broad option 4.2(b) and those discussed generally under 4. In addition, it can be assumed that compliance is most likely under this option as it includes an additional oversight body. It can be expected that the existence of such an oversight body and potential sanctions could incentivise companies to comply with their due diligence requirements regarding social matters. Therefore, it is expected that this sub-option increases the likelihood that the expected social impacts materialise. However, as discussed previously, this also depends on whether and how far social impacts are specified in the requirements. Same as in option 4.3(a), in the case that such remedies would pose a very high economic burden for companies, in theory this could have a negative impact on employment levels.

Impact on Human Rights

The large majority of stakeholders considered that new regulation requiring mandatory due diligence could have positive human rights impacts. Over 60% of respondents expect positive impacts on all human rights areas, and the top areas – with above 80% of responses- are the right to freedom from slavery, the rights of the child, women's rights, the right to non-discrimination/equality, the rights of indigenous persons, and the right to life, liberty and security of person. Additionally, most surveyed companies considered that new regulation requiring mandatory due diligence could have positive impacts on their supply chains. Over 60% of respondents expect positive impacts on 9 out of the 15 human rights areas, and the top areas – with above 70% of responses- are the right to freedom from slavery, the rights of the child, and women's rights.

However, out of the 19 sectors surveyed, in only four areas did a majority of companies confirm that they foresee mandatory due diligence requirements to have a positive impact on human rights. However most economic sectors stated that mandatory due diligence requirements would indeed have an impact down their supply chains to improve the human rights situation. The discrepancy may be founded in the simple notion that any plausible impacts on human rights depend on the scope of the mandatory directive, and how many companies will unquestionably fall under its mandate. This is demonstrated by the results of the EU Impact Assessment of Directive 2012/18/EU –

[1466] Quantification of compensation awards are usually based on the damages suffered by the claimants, unless pecuniary damages are awarded based on the bad faith or deliberately harmful conduct of the defendent.

Seveso III Directive[1467] as the level of human rights impacts by every policy option investigated was dependent on whether it would successfully cause an increase in the number of establishments under its direction or a decrease. Where there is a decrease in the number of establishments under the legislation, this might lead to a decrease in human and environmental health protection. However, where there is an increase in scope, this would lead to an increase in protection.

There is also a considerable amount of uncertain responses from stakeholders as to whether mandatory due diligence would have a positive impact on human rights. This may likewise be linked to the notion that mandatory requirements may put a company at risk, which is also reflected in the Market Practices section, where companies have expressed a concern that current due diligence practices may expose them to risks of litigation.

As such, it is unsurprising that low levels of compliance go hand in hand with difficulties in enforcing due diligence standards. A study conducted by Global Witnesses and Amnesty International showed that many US companies are failing to comply with the mandatory 2010 Dodd Frank Act. More specifically, the study analysed 100 conflict minerals reports filed by US companies in response to the Act. This analysis found that 79 of these companies failed to meet the minimum requirements established by the law, that only 16% of them were going beyond their direct suppliers to attempt to contact those down the production chain, and that more than half of the companies sampled did not report to senior management when they identify a risk in their supply chain. This is in line with the findings of the EU Assessment of Due Diligence Compliance Cost, Benefit and Related Effects on Selected Operators in Relation to the Responsible Sourcing of Selected Minerals (2014)[1468]. When assessing possible impacts of Option 4 which requires mandatory legality certification, the study found that the full reach of possible benefits may be put at risk as companies may seek the easiest, least risky and burdensome way of complying (avoiding sourcing from conflict-affected regions). This could trigger negative impacts on local communities as mineral flows could be diverted towards companies with lower standards and norms.

Moreover, a 2018 study demonstrates that even when companies do look beyond their direct suppliers, audits that certify suppliers as compliant, even independent and high-quality ones, are not sufficient to ensure that an approach is credible and has any benefits for rights-holders (German Watch: Sydow J. & Reichwein A., 2018). The study communicates that none of the assessed due diligence initiatives or guidelines for the mineral sector met 100% of the criteria developed by German Watch to define it as fully credible and transparency. When investigating down the supply chain beyond their direct suppliers, requirements may incentivize companies to rely on faulty certification schemes given to indirect suppliers as a confirmation of compliance. The concern of illegitimate credibility via faulty certification was reiterated by the European Commission Impact Assessment on Additional Options to Combat Illegal Logging (2008)[1469,1470] as Option 4B,

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[1467] See COMMISSION STAFF WORLING PAPER. IMPACT ASSESSMENT Accompanying document to the Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on the control of major-accident hazards involving dangerous substances. Available at: https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52010SC1590&from=EN [Accessed 11 Sep. 2019].

[1468] See European Commission (2014), Impact Assessment Accompanying the document Proposal for a Regulation of the European Parliament and of the Council setting up a Union system for supply chain due diligence self-certification of responsible importers of tin, tantalum and tungsten, their ores, and gold originating in conflict-affected and high-risk areas. PART 1 (Impact Assessment). Available at: https://eur-lex.europa.eu/resource.html?uri=cellar:b05a9c8f-a54d-11e3-8438-01aa75ed71a1.0001.01/DOC_1&format=PDF

[1469] See COMMISSION STAFF WORKING DOCUMENT Accompanying document to the Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL determining the obligations of operators who make timber and timber products available on the Market. IMPACT ASSESSMENT Report on additional options to combat illegal logging. Available at: https://ec.europa.eu/environment/forests/pdf/impact_assessment.pdf which requires legality certificates, runs the risk of accepting such certificates from countries which might be in violation of serious human rights abuses—and thus providing them with illegitimate credibility.

As such, the study concludes that a robust mandatory due diligence regulation such as the EU regulation on responsible mineral sourcing, or the US Dodd-Frank Act, must ensure that it restricts companies from trusting their suppliers on the basis of their certifications, and rather perform proper due diligence themselves to protect rights-holders.

While requiring companies to report on child labour practices and working conditions would naturally suggest a positive impact, compliance and transparency cannot be ensured. According to Nolan J. (2018), without any mechanism to encourage compliance with the legal requirements of transparency and due diligence, the uptake by companies of due diligence requirements may be limited. This has played out in practice via the implementation of the Modern Slavery Act in the UK. The introduction of civil (and criminal) penalties where human rights violations have occurred would significantly strengthen requirements.

Mandatory due diligence requirements risk suffering from low levels of effectiveness if exposed to issues of certification quality, compliance, and additionally because companies may not perceive due diligence requirements to prioritize risks *to rights-holders* but rather prioritize risks *to the company*. After its mission to Brazil in 2015, a United Nations working group report concluded that "human rights risks were mainly seen as risks to a company's operations, rather than risks faced by vulnerable rights-holders"[1471].

However, while recognizing challenges in real impact for rights-holders, evidence does demonstrate that legislation can be designed in such a way to restructure the balance of power and allow rights-holders to demand prioritization. For example, the European Commission's Report on the Implementation of the Environmental Liability Directive (2016), demonstrates that a key added value of the ELD refers to the recognition of stakeholder's rights under the directive. According to Articles 7(4) and 12 of the ELD, a person who could be affected by the damage, or with a legitimate interest, as well as environmental NGOs, have rights to request the implementation of prevention and remedial measures, by submitting the relevant information. The competent authority is obliged to evaluate the request and to notify the requestor of the decision.

In addition, mandatory due diligence requirements have significant benefits, even when less than 100% of companies comply. The Enough Project conducted field research in 2015 and 2016 in eastern Congo with miners, traders, human rights activists, civil society leaders, and foreign industry experts, to assess impacts of the Dodd-Frank Act. The investigation found direct positive impacts including increased security for civilians in some mining areas and a significant reduction in armed group control in 3T mining areas. Additionally, a few indirect advances for rights-holders were found around improved safety and health standards for miners, and the implementation of a regional certification system for mines as conflict-free. When 193 mines were assessed under this certification

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[1470] Indufor (2008). Assessment of the impact of potential further measures to prevent the importation or placing on the market of illegally harvested timber or products derived from such timber. Final Report. [online] Helsinki, Finland: Indufor in association with European Forest Institute (EFI). Available at: https://ec.europa.eu/environment/forests/pdf/ia_report.pdf [Accessed 10 Sep. 2019].

[1471] Turke M. (2018). Business and Human Rights in Brazil: Exploring Human Rights Due Diligence and Operational-Level Grievance Mechanisms in the case of Kinross Paracatu Gold Mine. Brazilian Journal of International Law. (Vol. 15, No. 2). DOI: 10.5102/rdi.v15i2.5357 scheme in Eastern Congo to investigate conflict and child labour, 166 of the mines (86%) successfully passed the assessment. Furthermore, according to the Enough Project (2015), the year 2015 saw a record amount of certified conflict-free tantalum exported from eastern Congo — a 387% increase since 2013. Moreover, looking at tin, tantalum, and tungsten mines together, 70% of those investigated by the International Peace Information Service in 2014 were conflict-free.

However, the high proportion of negative business responses, might also be explained by the notion that the impacts of poorly designed mandatory due diligence requirements may not necessarily be positive. The literature demonstrates that impacts for rights-holders could result in unintended consequences when mandatory due diligence obligations are imposed only for certain geographical regions, such as the Dodd Frank act, as this allows businesses to move to other areas of supply where these due diligence requirements do not apply. A study by the University of Texas School Of Law suggests, Section 1502 of the Dodd-Frank Act essentially created a de facto embargo on the entire mining industry in the DRC (Owen M., 2013). Companies found it simpler to withdraw from the area rather than to justify business associations with conflict. This sudden change caused the demand to drop by 90%, placing the economic burden on a vast population of civilians that depended on the income for their livelihood. According to the study, this has had negative impacts relating to the right to food, the right to education, and the right to health (Owen M., 2013). However, this phenomenon could presumably be linked to the mechanism’s narrow application to a specific geographical region, which allows for superficial circumvention of the requirements. This is less likely to apply if the due diligence requirements were imposed on a wider group of businesses operating globally.

2016 study by the University of Wisconsin-Madison confirmed this argument, outlining that while the conflict-minerals section of the 2010 Dodd-Frank Act has succeeded in its mission of decreasing the financing of warlords and conflict in East Congo, it also unexpectedly created a de facto boycott on mineral purchases. Estimating the impact on the mortality of children born before 2013, the study finds that it increased the probability of infant deaths in villages near the policy-targeted mines by at least 143 percent. Similar to the literature on burden allocation of economic sanctions, the paper suggests that the Act’s boycott reduced mothers’ means to purchase health care goods and services for their infants.[1472]

As such, the evidence of the efficacy of mandatory due diligence requirements seems to suggest that as long as robust risk assessment (based on those affected), transparency, monitoring, and compliance systems are enforced, and if the mechanism is designed to avoid unintended consequences, such as through wide standardisation to avoid circumvention, rights-holders can expect opportunities for protection.

Additionally, conditional on the definitions of offences, scope and enforcement mechanisms of Option 4, the extent of the identified benefits will differ according to the timeframe. Concerning short-term benefits, mandatory due diligence may result, for example, in the termination of contracts with suppliers that do not comply with the corresponding regulation. Moreover, if companies implement human rights due diligence framework comprehensively, in the mid to long term, they may benefit from

[1472] Dominic P. Parker & Jeremy D. Foltz & David Elsea, 2016. "Unintended consequences of economic sanctions for human rights Conflict minerals and infant mortality in the Democratic Republic of the Congo," WIDER Working Paper Series 124, World Institute for Development Economic Research (UNU-WIDER).

organisational learning that brings better business conduct with a focus on prevention rather than on remediation of harms[1473]. This may lead to competitive advantages based on an improved orientation towards stakeholders (communities, suppliers, customers and employees), that in turn may increase shareholder value as well as creating financial and social value in the long-term (i.e. sustainable business-models and supply chains)[1474].

Human rights impacts in third countries

The effects of mandatory due diligence for rights holders in third countries are dependent on the kind of business a company undertakes, the accountability and visibility of its actions in the home country, and the existing relationships with the surrounding community in the third country. Linked to the social impacts described above, positive impacts are particularly possible for the right to the highest attainable standard of physical and mental health for the effects on working conditions. Mandatory due diligence requirements would hold EU companies accountable to identify and rectify labour violations related to their global activities and possibly administered by suppliers in third countries.

However, as is evident with both effects at home as well as in host or third countries, the structure of the regulation will be particularly telling of its effectiveness. A poorly designed policy may see companies complying with the bare minimum. For example, companies have been found to extract water from a local source or polluting it remnants of production and thereafter simply ceasing its actions, but refraining from engaging in activity to properly replace the potable water source for the community. Finally, and perhaps one of the most concerning impacts on third countries, is the issue that while the regulation would intend to change EU firm behaviour both at home and abroad, companies under less stringent regulations in third countries might seek to leverage their position for a competitive advantage. However, the extent of this possibility is context-specific as a stronger regulatory environment may have regional effects and either pressurize governments in a host or third country to adopt similar legislation or hold companies in a host or third country accountable to follow suit voluntarily.

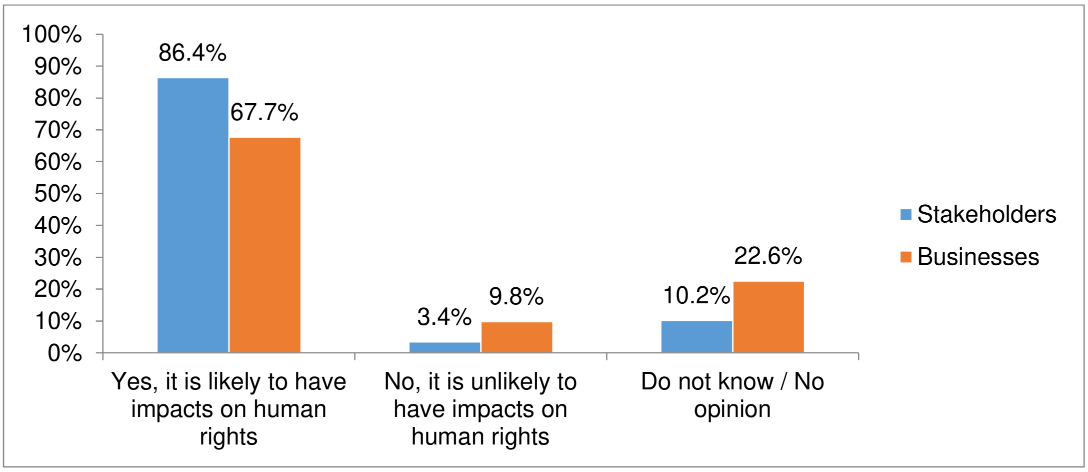
Expected human rights impacts

Stakeholders were asked about their perception on the effects that the introduction of mandatory due diligence requirements through the supply chain would have on human rights. While the majority of stakeholders (86.4%) expressed that it is likely that the introduction of mandatory due diligence requirements has an impact on human rights, although the difference on views with businesses was less notable in this case since (67.7%) of businesses also expressed that the requirement of mandatory due diligence is likely to impact human rights. A very small percentage of stakeholders (3.4%) expressed that the introduction of mandatory regulation would be unlikely to have an effect on human rights, while a higher percentage of businesses (9.8%) perceived that to be the case. Finally, (10.2%) of stakeholders answered that they do not know or do not have an opinion on the matter, while in the case of the businesses this percentage was (22.6%).

[1473] Buhmann, K. (2018). Neglecting the proactive aspect of human rights due diligence? A critical appraisal of the EU's non-financial reporting directive as a Pillar One avenue for promoting Pillar Two Action. Business and Human Rights Journal, 3(1), pp. 23-45. Available at: https://doi.org/10.1017/bhj.2017.24

[1474] Clark, G. L., Feiner, A., Viehs, M. (2015). From the stockholder to the stakeholder. How sustainability can drive financial outperformance. University of Oxford & Arabesque Partners. Available at: https://arabesque.com/research/From_the_stockholder_to_the_stakeholder_web.pdf

Figure 8.17: Expected human rights impacts under Option 4



Q29 Business Survey; 110 responses – Q24 Stakeholder Survey; 149 responses.

Specific impacts on human rights areas

The large majority of respondents – stakeholders and companies – who were of the view that mandatory due diligence requirements would have human rights impacts, considered that these impacts would be positive. Over 60% of respondents expect positive impacts on all human rights areas, and the top areas – with above 80% of responses- are the right to freedom from slavery, the rights of the child, women's rights, the right to non-discrimination/equality, the rights of indigenous persons, and the right to life, liberty and security of person. Similar to the previous alternatives, but with a smaller proportion, expectations of neutral impacts concentrate on the right to own property (27%), to privacy (25%), and to freedom from arbitrary arrest (22%). Very few (0% to 2%) of respondents expect a negative rather than positive or neutral impact.

Additionally, most companies who declared that the new regulation was likely to have some impact, considered that new regulation requiring mandatory due diligence could have positive impacts on their supply chains. Over 60% of respondents expect positive impacts on 9 out of the 15 human rights areas, and the top areas – with above 70% of responses- are the right to freedom from slavery, the rights of the child, and women's rights. Companies' expectations of neutral impacts are similar to stakeholder respondents. Neutral impacts concentrate on the right to privacy, the right to freedom from arbitrary arrest (47% respectively), and the right to own property (41%). Very few (0% to 3%) of respondents expect a negative rather than positive or neutral impact.

Table 8.57: Specific impacts on human rights areas (Option 4)

	Stakeholders				Businesses			
	Negative	Neutral	Positive	No opinion / don't know	Negative	Neutral	Positive	No opinion / don't know
Right to Life, Liberty and Security of Person	0.78%	8.59%	79.69%	10.94%	1.35%	16.22%	66.22%	16.22%
Right to Physical / Mental Health	1.58%	10.24%	77.96%	10.24%	1.37%	17.81%	64.39%	16.44%
Right to not be subject to Torture	0.00%	13.49%	78.58%	7.94%	1.37%	16.44%	65.76%	16.44%
Right to Freedom of Opinion/Expression	0.00%	17.32%	74.81%	7.87%	0.00%	27.40%	57.54%	15.07%
Right to Non-Discrimination / Equality	1.58%	6.35%	84.13%	7.94%	0.00%	20.55%	68.50%	10.96%
Right to own Property	0.79%	26.98%	59.53%	12.70%	1.37%	41.10%	36.99%	20.55%
Right to freedom from Slavery	1.58%	3.15%	88.19%	7.09%	1.37%	12.33%	76.72%	9.59%
Right to Freedom from	0.79%	22.05%	66.14%	11.02%	0.00%	31.51%	46.58%	21.92%

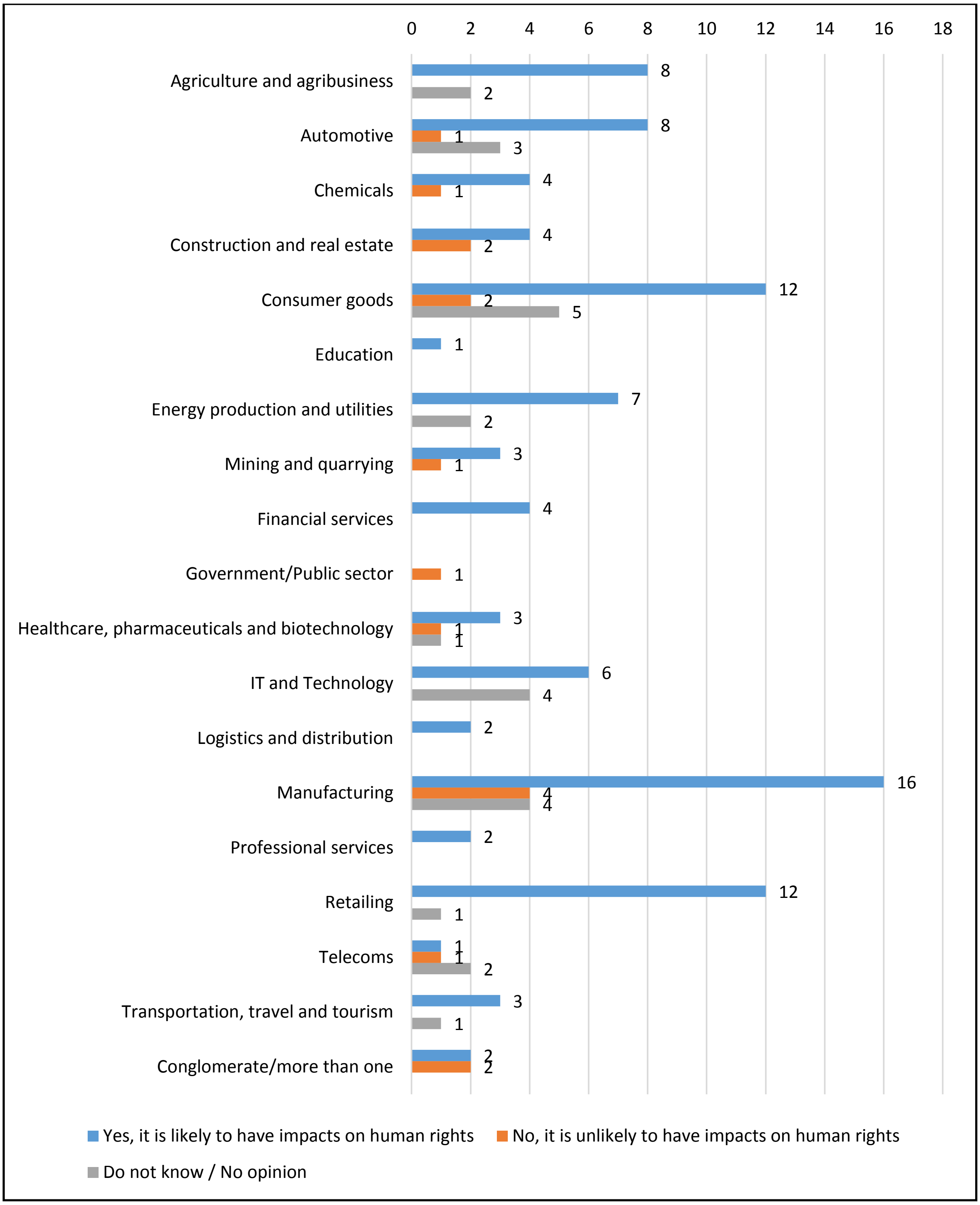
Arbitrary Arrest								
Right to Privacy	0.79%	25.40%	61.91%	11.90%	0.00%	31.51%	46.58%	21.92%
Right to Peaceful Assembly / Association	0.79%	11.81%	77.95%	9.45%	0.00%	23.29%	64.39%	12.33%
Right to Education	0.81%	16.94%	70.97%	11.29%	2.78%	23.61%	54.17%	19.44%
Rights of the Child	0.79%	3.97%	87.30%	7.94%	2.82%	12.68%	71.84%	12.68%
Women's Rights	0.00%	5.65%	87.09%	7.26%	2.74%	15.07%	71.24%	10.96%
Rights of Indigenous Persons	0.00%	9.52%	83.33%	7.14%	1.35%	21.62%	59.46%	17.57%
Rights of People with Disabilities	0.00%	16.00%	73.60%	10.40%	1.33%	20.00%	57.33%	21.33%
Q43 Stakeholder Survey; 131 responses.					**Q50 Business Survey; 77 responses.**			

Other sub-options

This section provides an indirect assessment of the sub-options that consider different applications of mandatory due diligence according to company size and economic sector. Due to low response rate the results below are presented as absolute frequencies; results by specific human rights area are not included for the same reason. The sub-options are:

a. Sub-option 4.1: Narrow category of business (limited by sector)
b. Sub-option 4.2(a): Set of large companies
c. Sub-option 4.2(c): All business plus specific obligations only applying to large companies.

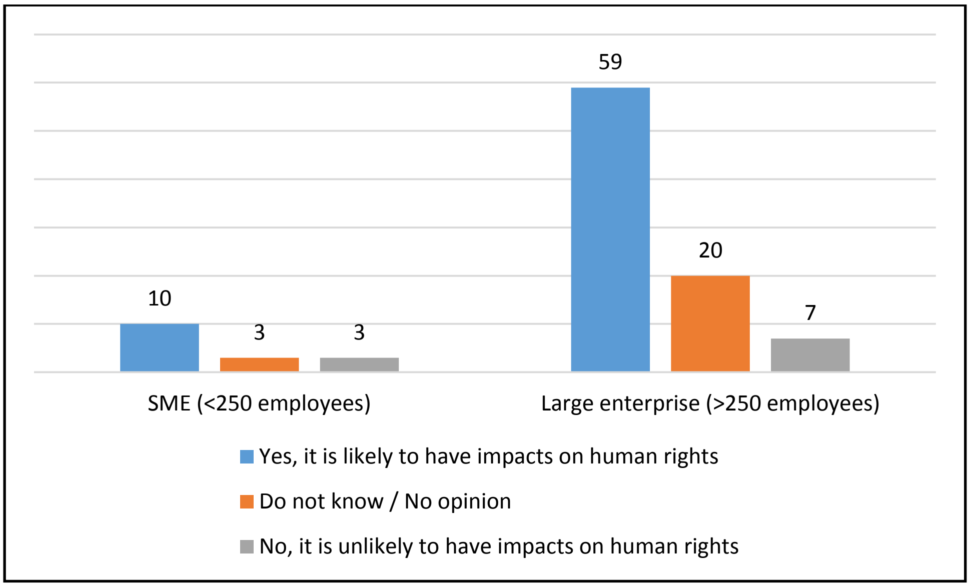
Figure 8.18: Expected human right impacts by economic sector under Option 4



Q49 Business Survey; 110 responses.

While the results above should be observed in recognition of their low response rates and implicative limitations, the few observations available do present an interesting story. There is a tendency to have positive prospects regarding the potential effects of mandatory due diligence among companies from the manufacturing sector, as well as among the retailing, agriculture and agribusiness, automotive and consumer goods sectors. The rest of the sectors follow a similar pattern, displaying consensus regarding the perception that Option 4 is likely to have impacts in human rights. The graph below shows a similar situation, amongst SMEs, most companies have favourable prospects regarding Option 4. Amongst large enterprises, the great majority shares these prospects.

Figure 8.19: Expected human rights impacts by company size under Option 4



Q49 Business Survey; 110 responses.

Environmental Impacts

This section presents the perceptions of companies and stakeholders regarding general and specific environmental impacts of the implementation of new regulation requiring mandatory due diligence as a legal duty of care. The questionnaire assessed this option in terms of a general application of mandatory due diligence without specifying any enforcement mechanisms or differential conditions according to company size or economic sector concerning environmental impacts.

Consequently, the following results review the application of the new regulation horizontally across sectors including all business regardless of company size. This alternative corresponds to sub-option 4.2(b). Additionally, to address the sub-options that consist of changing the scope of the requirements according to the economic sector and company size, the different environmental impacts are analysed according to these criteria. The expected environmental impacts of sub-options consisting of different enforcement mechanisms are not covered due to the data limitations mentioned above.

The new regulation requiring mandatory due diligence, which requires companies to carry out due diligence to identify, prevent, mitigate and account for actual or potential impacts is the most favoured option in terms of its potential effects on the environment. Most stakeholders and companies declare that they expect this alternative to have environmental impacts, but there are substantial differences between both types of stakeholders. A fifth of the participant companies do not expect environmental impacts, and a quarter does not declare an opinion, indicating, once more, uncertainty regarding the potential effects of this alternative.

Compared to the previous options – voluntary guidelines and required due diligence reporting – the expectations of positive environmental impacts are cleat cut among respondents. Among those who expect impacts associated to the new regulation, the vast majority in both groups indicate that Option 4 is likely to have positive effects on all the considered areas, particularly on the environmental air pollution and waste. Although there is a high level of coincidence between stakeholders' and companies' perceptions, some areas such as agricultural fertilisers and forests, show that the expectations of positive impacts are much higher among stakeholders. Additionally, companies refrain from giving an opinion in a higher proportion. These results are similar to the previous options, in which differences could be related to the specific sector where companies operate and the individual survey respondent's knowledge about the different areas considered to assess environmental impacts.

Because of data limitations, the situation for the sub-options is more difficult to determine. In general, large companies expect that new regulation requiring mandatory due diligence will have an impact on the environment, and the prospects are very similar across sectors, particularly in manufacturing and retailing. Despite showing a favourable disposition to mandatory due diligence, these results should be interpreted carefully as this option was presented to respondents without specifying conditions according to size, sector or enforcement mechanisms.

Aside from expected benefits regarding an increased engagement of companies with the environment and climate change, the literature has identified potential risks for compliance with more stringent environmental regulations. According to the literature, areas with lax environmental regulation, good market access to high-income countries and corruption opportunities – i.e. pollution havens – strongly attract polluting firms and significantly explain the location choice of polluting affiliates. This indicates that more demanding regulation such as Option 4, should consider additional market protection measures (e.g. a specific tax on imports), to discourage companies from taking advantage of pollution havens in order to reduce their compliance costs[1475].

Given that policy Option 4 applies to firms operating in the EU, companies would have to completely remove themselves from the European market in order to be exempted from liability in the case of non-compliance. Nevertheless, the risk of pollution havens lies in the criteria by which due diligence is deemed satisfactory rather than on relocation. According to the findings of the EU Assessment of Due Diligence Compliance Cost, Benefit and Related Effects on Selected Operators in Relation to the Responsible Sourcing of Selected Minerals (2014)[1476], the policy options that seek to establish mandatory legality certificates for sustainable mineral sourcing risk being ineffective. Companies may seek the easiest, least risky and burdensome way of complying with mandatory due diligence by avoiding sourcing from regions under such regulation. This could trigger negative impacts on the environment, as in this specific example, mineral flows could be diverted towards companies with lower environmental standards and norms (for example, upstream sourcing from suppliers that comply with laxer environmental regulation).

[1475] Candau, Fabien, and Elisa Dienesch. 2017. "Pollution Haven and Corruption Paradise". Journal of Environmental Economics and Management 85: 171-192. doi:10.1016/j.jeem.2017.05.005

[1476] See European Commission (2014), Impact Assessment Accompanying the document Proposal for a Regulation of the European Parliament and of the Council setting up a Union system for supply chain due diligence self-certification of responsible importers of tin, tantalum and tungsten, their ores, and gold originating in conflict-affected and high-risk areas. PART 1 (Impact Assessment). Available at: https://eur-lex.europa.eu/resource.html?uri=cellar:b05a9c8f-a54d-11e3-8438-01aa75ed71a1.0001.01/DOC_1&format=PDF

As such, the study concludes that a robust mandatory due diligence regulation must ensure that it restricts companies from avoiding stringent regulations by taking advantages of sourcing outside of the legislation's scope. In fact, investigating policy option 6, which implements an import ban for EU importers of ores that fail to demonstrate compliance with the OECD Guidance, the study demonstrates that positive impacts are most effectively delivered via increased government interventions to ensure that due diligence on environmental impacts is properly exercised. Therefore, the extent of risks posed by pollution havens – or countries with less stringent regulation regarding environmental and non-environmental matters – will depend on the definitions of offences and scope of liability of the chosen policy option.

Beyond domestic intervention, evidence, including results of the EU Impact Assessment of Directive 2008/99/EC on the protection of the environment through criminal law[1477] demonstrates that harmonisation of due diligence requirements across national boundaries, as well as with existing regulatory tools, can be expected to provide positive environmental impacts through increased sanction levels, offence definitions, and scope of liability. For example, the European Commission's Report on the Implementation of the Environmental Liability Directive (ELD), which establishes a framework based on the polluter pays principle to prevent and remedy environmental damage, is weakened by the fact that it is not coordinated or harmonised with the Habitats Directive. This allows for ambiguity and a fragmented interpretation of concepts such as *significant biodiversity damage* or *preventive and remedial measures* across Member States. As such damage or preventive methods cannot be properly measured, determining the extent of potential impacts, and establishing causal links is very difficult. While a key added value of the ELD is the possibility to attribute strict liability to an operator for damage to biodiversity, the distinction between "strict liability" and "fault-based liability" exists across different types of activities that are harmful for biodiversity. The result of this is that the procedures to prove causal links in the case of fault-base liability are exacerbated, and the implementation of the key accountability mechanism of the ELD is rendered impractical.

However, while recognizing challenges in real environmental impacts, evidence does demonstrate that mandatory due diligence requirements can be designed in such a way to have significant benefits, even when under 100% of companies comply. The EU Timber Regulation is perhaps one of the most notable regulations for its milestone binding characteristic as well as its successful implementation. The 2016 EUTR Evaluation indicates that the regulation proved to be highly relevant for tackling illegal logging and related trade by changing market behaviour patterns and freeing supply chains from illegally harvested timber. It is recognised as an important instrument to halt deforestation and forest degradation, enhance and maintain biodiversity, and address global climate change. Additionally, the report highlights the EUTR's added value of establishing uniform rules, and its coherence with other relevant policy instruments (VPAs, FLEGT AP, and the EU Wildlife Trade Regulations).

In sum, similarly to the conclusions addressed in the human rights impacts section for this policy option, the extent of the identified benefits will differ according to the timeframe, conditional on the definitions of offences, scope and enforcement

[1477] See COMMISSION STAFF WORKING DOCUMENT Accompanying document to the Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on the protection of the environment through criminal law. IMPACT ASSESSMENT. Available at: https://ec.europa.eu/smart-regulation/impact/ia_carried_out/docs/ia_2007/sec_2007_0160_en.pdf [Accessed 11 Sep. 2019].

mechanisms of Option 4. Outcomes such as termination of contracts or change of supplier and partners up and downstream the supply chain correspond to more immediate results likely to happen in the short to mid-term (provided that those suppliers/partners do not change their own practices). Other impacts such as the development of sustainable business models and the establishing of organisational learning strategies to implement a comprehensive due diligence strategy across units are outcomes likely to evolve in the mid to long term, together with the competitive advantages and shareholder value maximisation linked to these processes[1478,1479]. These potential long-term positive outcomes are particularly important given the risk posed by companies that source from countries with less strict regulation (as shown by interviewees concerns regarding offshoring harmful practices), because they may serve to counterbalance these risks, or even help overcome them if the future regulation prioritises a focus on prevention, provides legal certainty, and is consistent with existing requirements.

As demonstrated by survey responses as well as extensively in the literature, while EU companies are already concerned of the ETS's effects on carbon leakage, differences in further carbon regulation between regions fuel concerns about competitiveness. Mechanisms to tackle competition issues may improve environmental effectiveness and public support of such measures not just within the EU, but by setting a good example, around the world. However, possible solutions will require context and sector-specific considerations as drawbacks and trade-offs will be inevitable.

While numerous solutions have been proposed, three overarching options are commonly proposed: 1) offsetting net carbon costs of domestic production; 2) border-alignment mechanisms; and 3) establishing global regulations to equalize costs. While analysing the various policies to mitigate competition issues is out of scope for the analysis on environmental impacts, it can be noted that each comes with its own set of challenges, particularly the latter as history is spotted with difficulties in reaching global agreements. However, the second solution consisting of border-alignment mechanisms, is of specific interest to mitigate possible competitiveness impacts deriving from mandatory due diligence regulation. While typically suggested to offset competition issues under the EU ETS, compensating carbon intensive industries for the costs of switching from high emission suppliers to low emission options to comply with mandatory regulation has been suggested to be effective in levelling borders (CarbonTrust, 2010).

Environmental impacts in third countries

Similary to the effects on rights holders, environmental effects of mandatory due diligence in third countries are dependent on the kind of business a company undertakes, the accountability and visibility of its actions in the home country, and the existing relationships with the surrounding community in the third country. Mandatory due diligence requirements would hold EU companies accountable to identify and rectify environmentally damaging activities related to their global activities and possibly administered by suppliers in third countries.

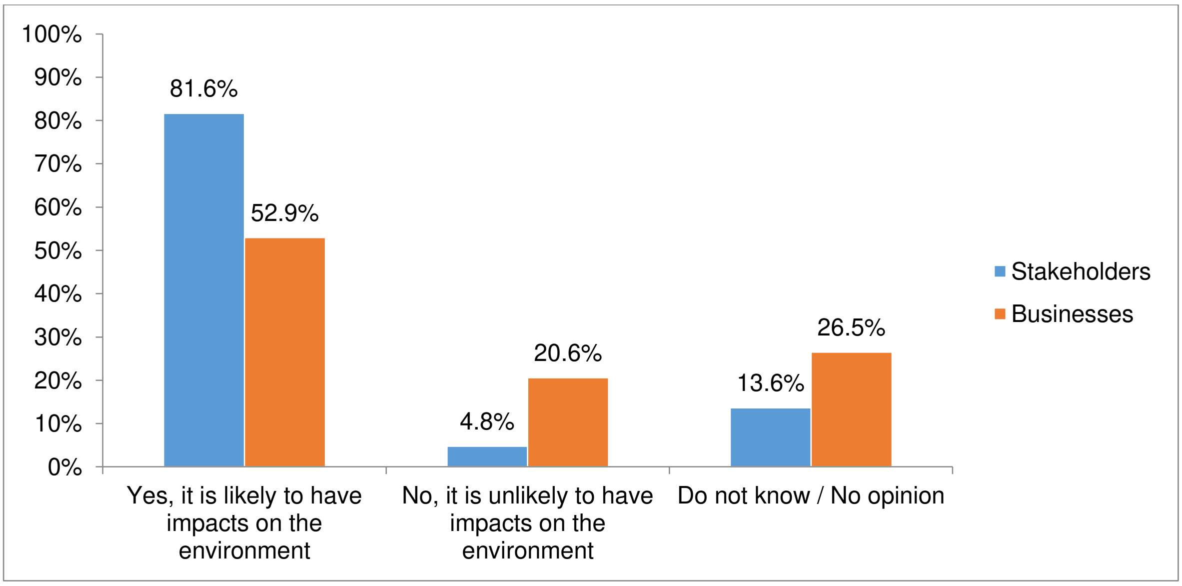
[1478] Clark, G. L., Feiner, A., Viehs, M. (2015). From the stockholder to the stakeholder. How sustainability can drive financial outperformance. University of Oxford & Arabesque Partners. Available at: https://arabesque.com/research/From_the_stockholder_to_the_stakeholder_web.pdf
[1479] See also Mohammed, M. (2013). Corporate accountability in the context of sustainability - a conceptual framework. *EuroMed Journal of Business*, 8(3), 243-254.

However, the structure of the regulation will determine its effectiveness as companies may seek to comply with the bare minimum under a poorly designed policy. Given that policy Option 4 applies to firms registered and operating in the EU, the issue of pollution havens is not directly related to the impacts of EU companies on third countries, and it is unlikely that companies would completely remove themselves from the European market in order to move activities to such locations. However, risks lie in a reduction of EU company presence in pollution havens translating into an increase of companies with laxer regulations. On the other hand, mandatory due diligence requirements from EU companies could also have the opposite impact and facilitate the implementation of stricter enviornmental regulations in host countries and thus support creating a level-playing in the host or third country of the supply chain company. Even if stricter legislation is not passed in third countries, stronger environmental due diligence amongst EU companies may have spill over effects as EU companies will ideally be sourcing from suppliers that meet their environmental obligations and thus companies in host or third companies may voluntarily increase compliance with environmental regulation out of their jurisdiction due simply to competitiveness.

Expected environmental impacts

A substantial percentage of stakeholders (82%) answered that the introduction of mandatory due diligence requirements in the regulation is likely to have impacts on the environment, a smaller percentage (53%) of companies declared to agree with that statement. On the other hand, only 5% of stakeholders perceived that inserting new regulations with mandatory due diligence would unlikely have an impact on the environment, while 21% of businesses expressed this point of view. Finally, those who did not know or who did not have an opinion on whether mandatory regulations would have an impact on the environment amounted to (14%) in the case of stakeholders, rising to (27%) for companies. The percentage of answers per category differed markedly between stakeholders and business responders.

Figure 8.20: Expected environmental impacts under Option 4



Q47 Business Survey; 102 responses – Q40 Stakeholder Survey; 147 responses.

Specific impacts by environmental area

The vast majority of respondents who anticipate environmental impacts from mandatory due diligence regulation expect these effects to be positive for all the areas related to the environment. In the case of general stakeholders, over 70% foresee positive impacts in the different areas, except for transport (64.8%) which shows a slightly higher proportion of no opinion compared to the other areas. Most companies also expect positive impacts; however, they are between 55%-65% and tend to indicate that they have no opinion/do not know more often than stakeholders. As for the previous options, the most relevant areas in terms of potential positive effects are environmental air pollution (68.9% of companies and 77% of stakeholders) and waste (71% and 77% respectively). The areas where there are divergent views between stakeholders and companies are agricultural and fertilisers (80% versus 56%), fisheries, forests and greening of the economy (differences between 15% and 24% between stakeholders and companies). In general, a tiny proportion of participants foresee negative impacts across the different areas, particularly among stakeholders.

Table 8.58: Specific impacts by environmental area (Option 4)

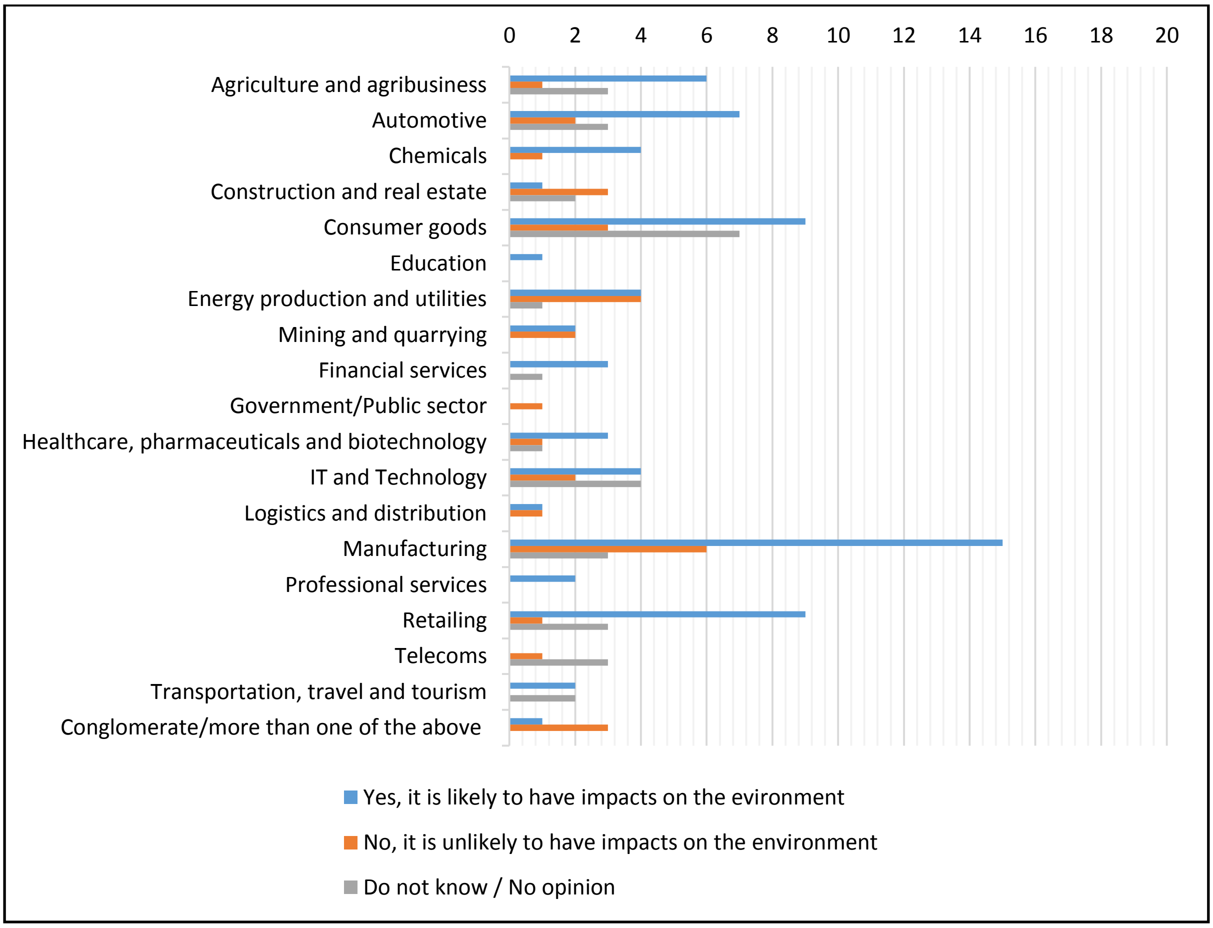
	Stakeholders				Businesses			
	Negative	Neutral	Positive	No opinion / don't know	Negative	Neutral	Positive	No opinion / don't know
Environmental Air Pollution	0.8%	7.9%	77.0%	14.3%	1.6%	9.8%	68.9%	19.7%
Waste	0.8%	6.5%	76.6%	16.1%	1.6%	6.5%	71.0%	21.0%
Energy use and mix	0.8%	9.0%	71.3%	18.9%	1.6%	12.9%	64.5%	21.0%
Transport	0.0%	14.8%	64.8%	20.5%	1.6%	14.8%	60.7%	23.0%
Water Resources	0.0%	8.1%	78.9%	13.0%	1.6%	13.1%	67.2%	18.0%
Biodiversity	0.0%	9.5%	73.8%	16.7%	1.6%	14.8%	55.7%	27.9%
Agricultural Fertilisers	0.0%	8.0%	80.0%	12.0%	1.6%	14.8%	55.7%	27.9%
Forests	0.0%	11.2%	76.0%	12.8%	1.6%	11.5%	59.0%	27.9%
Fisheries	0.0%	12.8%	71.2%	16.0%	0.0%	16.4%	47.5%	36.1%
Greening of the Economy	1.6%	8.1%	73.2%	17.1%	1.6%	14.1%	57.8%	26.6%
Q41 Stakeholder Survey; 128 responses.					**Q48 Business Survey; 65 responses.**			

Other sub-options

This section provides an indirect assessment of the sub-options that consider different applications of mandatory due diligence according to company size and economic sector. Due to low response rate the results below are presented as absolute frequencies; results by specific environmental area are not included for the same reason. The sub-options are:

a. Sub-option 4.1: Narrow category of business (limited by sector)
b. Sub-option 4.2(a): Set of large companies
c. Sub-option 4.2(c): All business plus specific obligations only applying to large companies.

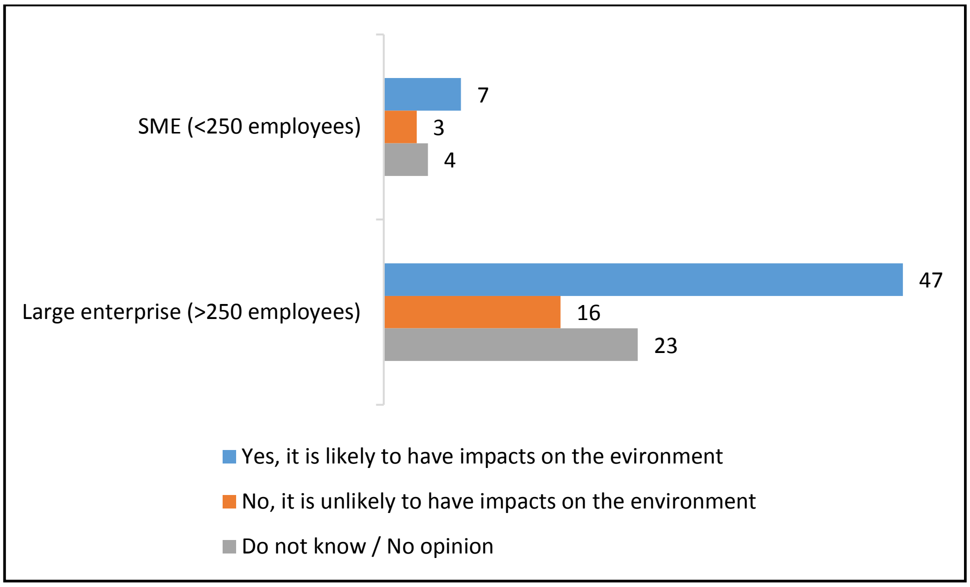
Figure 8.21: Expected environmental impacts by economic sector under Option 4



Q47 Business Survey; 102 responses.

Considering economic sectors with larger response rates, there is a tendency to have positive prospects regarding the potential effects of mandatory due diligence among companies from the manufacturing sector, as well as among the retailing, agriculture and agribusiness, automotive and consumer goods sectors. In the rest of the sectors, responses indicating that impacts are unlikely are almost as frequent as those indicating that they do expect impacts from mandatory due diligence.

Figure 8.22: Expected environmental impacts by company size under Option 4



Q47 Business Survey; 102 responses.

Within the group of small and medium-size companies, responses indicating that the new regulation is likely to have an impact on the environment are more frequent. However, responses declaring the opposite or uncertainty have the same frequency. The situation amongst large companies is clearer, more than half of respondents declare that it is likely that mandatory due diligence will have an impact on the environment. Responses such as do not know / no opinion are more frequent than those who indicate that no impact is expected.

It must be noted that the sub-options that were assessed in the survey did not inform the respondents about specific obligations or scopes of application regarding size or sector. However, these results can be interpreted in light of the current context.

In particular response to the Paris agreement in 2015, companies have begun adopting ambitious emissions reduction targets to ensure the transformational action undertaken in response to environmental regulation is aligned with current climate science. In order to be considered "science-based", company targets must align with what scientists urge is necessary to comply with the Paris Agreement. Thus far, 732 companies have committed to undertaking science-based climate action.[1480]

There is a recent and substantial increase of litigation intended to hold actors accountable for failures to tackle foreseeable impacts on the environment and climate change. On the one hand, the upsurge of climate-related court cases reveal essential discrepancies between the companies' internal knowledge of their contribution to harmful activities or emissions and the external communications of these issues. The high uncertainty displayed by companies regarding their perception of the potential effects of mandatory due diligence could be reflecting this gap of knowledge and pointing out the need of increasing the engagement of companies with environmental and climate-related issues regardless of the economic sector.

[1480] See https://sciencebasedtargets.org/companies-taking-action/.

On the other hand, there are hardly any successful court cases related to climate justice that have been resolved against companies. In line with these developments, the Report of the Special Rapporteur on extreme poverty and human rights, 'Climate change and poverty'[1481] denounces the governmental complicity with corporate damages and their failure to promote compliance with the different existing regulations. It emphasises the need for mechanisms that hold companies accountable for their negative impacts as well as implementing transformative approaches to mitigation of environmental impact and climate change.

As indicated in the climate change section included in the Regulatory Review, our survey and the interviews showed that climate change due diligence is rarely a self-standing process within companies. Interviewees' views also show the existence of a silos mentality when they explain that the alignment of climate change goals or strategies are not shared company-wise but allocated in specific departments or units. These results are in line with a recent literature review on reporting and use of non-financial data in the EU which shows, for example, that out of 80 top-listed companies, only 20% include a specific climate change policy section, and 30% report greenhouse gas emissions targets.[1482]

In this context, the potential benefits of Option 4 regarding climate change are linked to those effects that relate to the improvement in the specific environmental areas detailed in the survey results (such as air pollution, waste, energy use, among others). From the interviewees' point of view, an enhanced business conduct concerning the prevention, protection and reduction of environmental harm that results in meeting climate change goals such as those stipulated in the Paris Agreement, require a regulation that prompts comprehensive due diligence processes (e.g. due diligence of corporate projects including the environmental practices of the companies' affiliates, and internal awareness processes to maintain continuous assessment of existing and potential actions to assist in limiting global warming).

It must be noted that steps to implement due diligence that includes climate-related issues are relatively new. The most salient ones so far correspond to the OECD Guidance on Responsible Business Conduct, and the EU NFRD. These are characterised by complementing environmental and human rights domains acknowledging their interrelationship. Both domains intersect in the following main dimensions: the environment as a prerequisite for the enjoyment of human rights; specific human rights that are essential for good environmental decision-making; and the right to a safe, healthy and ecologically-balanced environment as a human right itself.[1483] Taking these into account, environmental due diligence – always conditional on its definitions, scopes and enforcement – has potential impacts on making progress towards climate-related targets as long as it is coherent with the recent guidelines and directives that frame the environment and human rights issues as complementary, prompting organisations to address them as part of systemic due diligence processes.

[1481] Office of the United Nations High Commissioner for Human Rights. 2019. "Report of the Special Rapporteur on Extreme Poverty and Human Rights. Climate Change and Poverty." Retrieved from: https://www.ohchr.org/EN/HRBodies/HRC/RegularSessions/Session41/Documents/A_HRC_41_39.docx

[1482] Juergens, I., Erdmann, K. (2019). A short qualitative exploration of the reporting and use of non-financial data in the context of the fitness check of the EU framework for public reporting by companies. Report prepared for the European Commission by DIW Berlin (In press).

[1483] UNEP. (2019). Human Rights and the Environment. [online] Available at: http://web.unep.org/divisions/delc/human-rights-and-environment [Accessed 29 Oct. 2019].

Impacts on Public Authorities

This option would most likely entail the same activities for public authorities as option 3, i.e. an external study to draft an implementation guidance and an ex post study on the implementation. However, if any monitoring is to take place at EU level, the expected personnel cost for staff at the EC to monitor and assess the implementation would most likely be much higher, as the monitoring activities would go beyond assessing sample reports. Monitoring activities would require EC or staff or external auditors to look into selected companies' supply chains.

In order to be "mandatory", sub-options 4.1 and 4.2 would need to be accompanied by legal sanctions or liability for failure to comply. Therefore, option 4 implies higher costs than earlier options for the state-based oversight and judicial systems in EU Member States, depending on the sub-option and the chosen oversight and enforcement mechanism.

Sub-option 4.1: Narrow category of businesses (limited by sector)

Due to the lack of existing legislation, it is difficult to estimate costs for public authorities, particularly against the background that it is unclear to which and how many industry sectors a new regulation would apply. If the latter would apply to large industries or various sectors, more companies would have to comply with the regulation. The greater the scope of companies or sectors, to the more compliance controls and inspections of companies are required to ensure high compliance rates. This could increase the costs for public authorities. As the coverage of industry sectors of the regulation remains yet unknown, possible costs described below need to be read with reservations.

Implementation, monitoring and enforcement of the regulation is most likely to take place at Member State level. However, if any monitoring or enforcement were to take place at EU level, it can be expected that this option would – similar to option 3 – require personnel costs for staff at the EU to provide implementation guidance and conducts sample reviews.

To ensure an effective implementation of a mandatory regulation it would also be necessary to provide personnel at Member State level in designated control bodies to conduct and coordinate compliance controls and inspections in each Member State. According to the estimations from the Impact Assessment regarding the Conflict Minerals Regulation for the assessed mandatory regulatory options, such personnel costs can be estimated around 1.5-2 FTE per EU Member State. Based on Eurostat data for average labour costs and average working hours per week, this could result in a yearly average labour cost of per EU MS of 81 300 EUR (1.5 FTE) to 108 400 EUR (2 FTE) and a total average labour cost for the EU-28 of approximately 2.276 to 3.034 million EUR (for 1.5 and 2 FTE, respectively).

Table 8.59: Average labour costs (EUR), in 2018 based on EU-28[1484]

Average hourly	Average monthly	Average yearly labour costs for 1.5	Average yearly labour costs for 2

[1484] Average monthly labour cost were calculated based on average hours worked per week of full-time employment for the EU-28 in 2018 and a 4-week month. Source: https://ec.europa.eu/eurostat/databrowser/view/tps00071/default/table?lang=en.

labour costs	labour costs	FTE	FTE
27.4	4515.52	81279.36	108372.48
Source: Eurostat, Indicator: Labour costs annual data - NACE Rev. 2[1485]			

It has to be noted, however, that these labour costs differ substantially between different Member States and that these averages are averages across different types of professions not public servants which can be expected – especially when employing highly specialized posts such as in this case – to be causing higher than average labour costs. Furthermore, it has to be pointed out again that the Conflict Minerals Regulation is only applicable to specific conflict-related risks in a limited sector, so it can be assumed that costs would be higher for a regulation with a wider scope.

In addition, it can be expected that additional costs may be created due to coordinative management committee meetings with representatives from the European Commission and the Member States, which are estimated at 60,000 EUR if taking place twice a year and 120,000 EUR if taking place four times a year.[1486]

Sub-option 4.2: Horizontally across sectors

The initial cost to set up structures and processes to monitor the implementation of a new mandatory regulation would be similar regardless of the number of companies affected by a new regulation. However, the expected operating costs for sub-options 4.2(a) to 4.2(c) might differ slightly according to the number of companies which may be covered by the regulation. As discussed under sub-option 4.1, the more companies would be liable to the regulation, the more costs it may create for public authorities as they may need to conduct more compliance controls and inspections of companies.

Sub-option 4.2(a): Set of large companies

The cost of this sub-option depends on the number of companies to which the new regulation would apply. Given that 99% of EU companies are SMEs (enterprises employing less than 250 people)[1487], it can be expected that this sub-option would only apply to 1% of EU companies. However, this would depend on the definition of large companies and/or the definition of the affected group of companies. It is also noted that a significant number of these SMES are within the supply chains or value chains of the 1% of large companies. Insofar as the regulation would extend to due diligence through the supply chain, the standard of care required would indirectly apply to the practices of these SMEs through the large companies with which they do business.

[1485] Average hourly labour costs are defined as total labour costs divided by the corresponding number of hours worked by the yearly average number of employees, expressed in full-time units. Labour Costs (D) cover Wages and Salaries (D11) and non-wage costs (Employers' social contributions plus taxes less subsidies: D12+D4-D5). Source: https://ec.europa.eu/eurostat/databrowser/view/tps00173/default/table?lang=en.
[1486] See the Conflict Minerals Regulation Impact Assessment.
[1487] Eurostat (2018). Statistics on small and medium-sized enterprises. Available at: https://ec.europa.eu/eurostat/statistics-explained/index.php/Statistics_on_small_and_medium-sized_enterprises.

Sub-option 4.2(b): All business, including SMEs

The cost of this option may be slightly higher than the cost expected for option 4.1 since under this option the regulation would apply to all companies in the EU, independent of their size or sector. As indicated before, it can be expected that initial costs for setting up structures and processes would remain the same, but monitoring and coordination activities may increase if more compliance controls and inspections would be carried out as a result of the larger number of companies covered by the new regulation. This may require more personnel at the European Commission for the monitoring of the implementation and sample reviews, as well as more personnel to coordinate compliance controls and inspections in each Member State**.**

Sub-option 4.2(c): All business plus specific additional obligations only applying to large companies

The cost of monitoring additional obligations for large companies would depend on the type of additional obligations and whether this would require additional staff and/or additional processes and structures. For example, in this study we describe the example of requiring large companies to undertake additional due diligence steps relating to climate change with reference to the Paris Agreement.

Since the Paris Agreement is a state-to-state agreement, any new regulatory due diligence standard which requires additional measures from (large) companies in relation to the Paris Agreement would need to clarify what such expected steps would be. For example, if recent developments discussed in the Regulatory Review, including the OECD NCP case against ING, are used as an indication of how this due diligence requirement may develop, additional requirements for large companies may refer to target-setting, measuring and reporting on climate change impacts. In accordance with this mixed sub-option these expectations would be automatically imposed on certain large companies by virtue of their size and regardless of their climate change risks, and would not be applicable to smaller companies unless they have specific climate change risks.

Depending on the level of oversight which is already provided at Member State level for the monitoring of companies' climate change impacts, additional obligations relating to specific target-setting, measuring steps and reporting on companies' approaches, as well as their strategies and challenges for low-carbon developments, it is expected that additional obligations relating to specific target-setting, measuring and reporting on climate change impacts may create additional measuring and oversight resources at Member State level.

Sub-option 4.3: Sub-options 1 and 2 accompanied by a statutory oversight and / or enforcement mechanism

In order to be "mandatory", sub-options 4.1 and 4.2 would need to be accompanied by legal sanctions or liability for failure to comply. The potential cost implications of these enforcement options are discussed in sub-options 4.3(a) or 4.3(b) below.

It is also noted that these enforcement or liability mechanisms set out in sub-options 4.3(a) and 4.3(b) are not mutually exclusive, and Member States may make provision for both in their implementation of the EU standard. Accordingly, it can be expected that Option 4 could create significant additional costs for public authorities and the legal systems in EU Member States.

Given the lack of empirical evidence from similar legislative initiatives, which are all relatively recent, the cost for potential elements of sub-option 3 is not possible to foresee, especially since the specific elements of a new regulation are not defined.

Even for relatively old laws such as the Environmental Liability Directive (ELD) from 2004 it is difficult to find estimates concerning the cost for public authorities. A report on its implementation[1488] states that only three Member States (Belgium, Bulgaria, Spain) provided precise data on administrative costs[1489] for public authorities, ranging from EUR 55 000 per year (in the Flemish Region of Belgium) to annual administrative costs of EUR 135,613 per year in Bulgaria and EUR 2 million (in some of the autonomous communities of Spain). As result of the limited information on administrative costs for authorities, the report concludes that it is not possible to draw sound conclusions on the administrative costs.

Sub-option 4.3(a): Mechanisms for judicial or non-judicial remedies

The additional cost of sub-option 4.3(a) would depend on whether judicial or non-judicial remedies under a new regulation would use existing judicial or non-judicial structures or whether it would require to establish new bodies and/or processes. If a judicial remedy is foreseen, it is expected that this would take place within existing judicial structures and processes so that this option would not create any additional costs for the legal systems of EU Member States. If non-judicial remedies are foreseen under a new regulation, the question of additional costs depends on the form of such non-judicial remedies and whether these would use pre-existing structures. Non-judicial remedies could take the form of specially created tribunals, which may create additional costs depending on their nature (private or public), but could also consist of having resort to existing administrative bodies or ombudsmen.

Sub-option 4.3(b): State-based oversight body and sanction for non-compliance

As described in the Problem Analysis and Regulatory Options, an oversight and enforcement body could either be established within existing departments and or a new body could be created. If a new body would need to be created, additional costs for public authorities would be significantly higher compared to financing additional staff within existing institutions such as a state department dealing with company law. However, even if existing structures are mandated with enforcement functions, this would most likely imply additional costs for training and expert staff who are familiar with human rights, environmental, climate change and related sustainability impacts in the supply chain.

Furthermore, it would depend on which law would be used for the enforcement (e.g. company or criminal law) whether such oversight bodies would need to be instituted at the national Member State level or whether it could be established at the EU level. If an

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[1488] Brussels, 14.4.2016 COM(2016) 204 final REPORT FROM THE COMMISSION TO THE COUNCIL AND THE EUROPEAN PARLIAMENT Report from the Commission to the Council and the European Parliament under Article 18(2) of Directive 2004/35/EC on environmental liability with regard to the prevention and remedying of environmental damage. Retrieved from: https://ec.europa.eu/transparency/regdoc/rep/1/2016/EN/1-2016-204-EN-F1-1.PDF. And COMMISSION STAFF WORKING DOCUMENT REFIT Evaluation of the Environmental Liability Directive Accompanying the document Report from the Commission to the European Parliament and to the Council pursuant to Article 18(2) of Directive 2004/35/EC on environmental liability with regard to the prevention and remedying of environmental damage. SWD/2016/0121 final. Retrieved from: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=SWD:2016:121:FIN

[1489] According to the report "administrative costs under the ELD are only those which are not borne by the liable operators, i.e. cannot be recovered from them. They relate for example to the manpower, equipment and other administrative costs which are – apart from the initial set-up costs at the beginning of the implementation – those continuous costs which cannot be recovered from liable operators (system maintenance and compliance promotion as outlined above)."

oversight and enforcement body would need to be established in each EU Member State, this would imply significant additional costs for public authorities in the Member States. The cost for such an oversight and enforcement body, independent of whether it would be established at Member State or EU-level, would also depend on its foreseen tasks, powers and the resulting requirements for the quantity and qualifications of specialized staff. Oversight and enforcement bodies could, for example, have extensive powers to grant orders and issue fines, or have investigatory powers such as issuing warrants, undertaking searches or issuing subpoenas. The more comprehensive such powers would be, the more extensive the tasks of such oversight bodies would be and the more staff with specialized qualifications would be needed.

Depending on which system of sanctions will be chosen for a new regulation on due diligence different costs may arise for public authorities. The EFFACE synthesis report discusses different systems of sanctions (administrative/criminal/civil) for the ECD. It provides an overview of the different types of approaches and sanctions to addressing environmental crime and briefly compares their cost impact for the state. The report concludes that under a criminal law approach costs for the State would be highest compared to an administrative approach or civil law suits (see Table 8.60 below).

Table 8.60: Expected costs for public authorities from criminal, administrative and civil law approaches to addressing environmental crime in EFFACE synthesis report

Criminal law approach	Administrative approach[1490]	Civil law suits
Costs of proceedings born mostly by state; relatively high costs for the state due, among others, to high threshold of proof and length/complexity of proceedings	Typically, lower costs for the state than in criminal proceedings, among others because of less complex proceedings	Relatively low costs for the state, but often high costs for the parties, as they are responsible for producing evidence

The Impact Assessment relating to the UK Bribery Act[1491] expects as a result of the new regulation one additional contested fraud and corruption prosecution per year and one additional contested criminal prosecution every three years. The costs of these additional court cases are estimated to range up to around 2 million British Pounds per year. However, if fines were issued to companies, this may also generate income for public authorities, which depending on the level of the fines, may cancel out or even outweigh some of the public costs for setting up new bodies and judicial proceedings.

The Impact Assessment relating to the EU Timber Regulation provides an estimate for the assessed option 5, which is a legislation requiring companies placing timber on the market to exercise due diligence in ascertaining that the products are legal. For this option the impact assessment expects regulatory costs from the "verification whether effective systems have been put in place by operators for ascertaining that the products are legal" and estimates regulatory costs in the EU of EUR 1 million per year. In how far

[1490] "Regarding terminology, it should be noted that what is referred to as administrative sanction or measure in most countries, may be a called a "civil sanction" or similar in common law systems like in the UK."

these estimates can be compared to the sub-options 4.3 depends on the final design of the regulation and whether similar activities would be foreseen for any oversight body.

The background analysis[1492] for the latest biennial implementation report[1493] of the EUTR provides information on the human and financial resources available to the Competent Authorities in each country for the implementation and enforcement of the EUTR. The indicated use of resources is based on the national reports by Member States. However, the quality and comparability of the reported data by Member States remains relatively low, which makes it difficult to draw general conclusions from the provided information. Under the EUTR the Competent Authorities in each country are required to put in place a plan for checks of operators and procedures for checks on Monitoring Organisations to verify their compliance with the EUTR. In this regard, it is important to point out that the applicability of the following figures depends crucially on the tasks which would be required by public authorities under a new due diligence regulation and in how far these tasks are similar or comparable to those required by the Competent Authorities under the EUTR.

For human resources, the background analysis report describes that for timber imported into the EU, available human resources of Competent Authorities ranged from 0.125 full time equivalent (FTE) staff to as many as 8 staff.[1494] Similarly, for domestic timber, available human resources varied between 0.125 FTE and 20 staff. For both estimates, i.e. for imported as well as domestic timber estimates, the relatively high number of human resources reported by Italy, Greece, Denmark and Bulgaria were taken out as outliers in the report.[1495] In addition, in many countries the core staff are also supported by others, who are not primarily focussed on EUTR implementation and enforcement (e.g. forest inspectors). The information on financial resources provided by Member States in their national reports shows even more variation and less comparability, which is why no concrete figures can be used as an approximation for potential financial costs arising for an oversight body. As shown in the detailed tables provided in the literature review section, some countries have reported extremely limited budgets for implementation and enforcement of the EUTR (e.g. Belgium), whereas others (e.g. Germany) reported that they did not have an upper limit.

Similarly, the Impact Assessment on the Seveso III Directive provides a cost estimate for competent authorities to make an in-depth site-by-site analysis of the concerned establishments. The described objective of such site-by-site analysis is to assess whether or not there are appropriate safety distances and to identify what remedial land-use measures might be needed. The total cost for this site-by-site analysis is estimated at more than EUR 130 million. Depending on the foreseen activities of an oversight body, if it would be required to also carry out such site-by-site analyses, this cost could incur for public authorities. It can be expected that the cost could be much higher for a new due diligence regulation, depending on the number of firms covered by the new regulation.

[1492] European Commission (2018). Background analysis of the 2015-2017 national biennial reports on the implementation of the European Union's Timber Regulation (Regulation EU No 995/2010). Retrieved from: https://ec.europa.eu/environment/forests/pdf/WCMC%20EUTR%20analysis%202017.pdf

[1493] European Commission (2018). Evaluation of Regulation (EU) No 995/2010 of the European Parliament and of the Council of 20 October 2010 laying down the obligations of operators who place timber and timber products on the market (the EU Timber Regulation). Retrieved from: https://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1538746572677&uri=COM:2018:668:FIN.

[1494] In the official biennial implementation report the upper estimation is 8 staff which seems to be the correct figure, compared to the indicated 10 staff in the background analysis.

[1495] The report states that the "relatively high number of human resources reported by Italy, Greece, Denmark and possibly others may be based on customs personnel or other supporting staff in general also having been included."

In the Seveso III Directive these requirements only apply for "upper-tier establishments", which consisted in 2011 of 4791 establishments.[1496]

3.2.3 Comparison of options and final assessment

- **Estimated Cost at Company Level**

For mandatory DD, our estimates indicate that a representative large company with revenues of 10 billion EUR would face additional annual labour cost of approximately 500,920 EUR. By comparison, for mandatory DD, our estimates indicate that a representative SME with revenues of 1 million EUR would face additional annual labour cost of approximately 740 EUR, while a large SME with annual revenues of 50 million EUR (the upper bound according the Eurostat SME definitions) would face additional annual labour cost of 36,990 EUR. Taking into account the additional burden resulting from new DD requirement, we consider our results to be in line with the findings of the impact assessment for the EU's Non-financial Reporting Directive.

- **Social Impacts**

Options 2 and 3 are expected to have only a minor positive social impact. This is due to the fact that both options do not require companies to take any due diligence actions but merely provide new guidance or require reporting similar to the existing EU NFRD. It is not expected that substantial actions would be taken by companies to address social matters as a result of these options. Both options are also expected not to have any major negative or positive impacts on employment levels. Negative impacts on employment are relatively unlikely since option 2 does not stipulate any requirements and the potential economic burden of the reporting requirements under option 3 would remain limited (depending though on the detailed requirements, coverage, enforceability, etc.).

Since option 4 is the most ambitious option and requires the most efforts from companies, it is the option from which social impacts are expected to be most significant. On the one hand, negative impacts on employment levels could arise if the economic burden for companies arising from the due diligence requirements is substantial. On the other hand, there could also be positive impacts on employment levels within and outside of the EU, especially in the long run. This could be the case if reputational effects lead to increased production and therefore increased demand for labour or if there is more demand for staff with specialised expertise resulting from due diligence activities. The magnitude of the social impacts depends on the application of the new regulation (the more companies affected, the higher the expected negative and positive impacts), the social issues which are expected to be addressed and specified by the regulation and thus to be covered by companies, and the effectiveness of an enforcement mechanism to ensure the implementation of due diligence practices.

[1496] According to the Commission Report on the Implementation of the Directive, "in December 2011, a total of 10314 establishments were reported, an increase over the reporting period of 3%, with 5523 lower-tier (54 %) and 4791 (46 %) upper-tier." Source: European Commission (2013). FROM THE COMMISSION Report on the Application in the Member States of Directive 96/82/EC on the control of major-accident hazards involving dangerous substances for the period 2009-2011. Retrieved from: https://circabc.europa.eu/sd/a/6e9ec4e2-89ae-404e-988c-1ff6effff1d6/1_EN_ACT_part1_v7.pdf.

- **Impacts on Human Rights**

While voluntary guidelines (option 2) raise awareness and provide rights-holders with a benchmark against which to hold companies accountable, they likewise risk being exploited by companies that advertise to be in line with guidance, but take no steps to actually implement it in entirety. Voluntary guidelines also inherently lack any kind of enforcement mechanism and rely on a company's willingness to comply and respect human rights duties. The analysis of voluntary guidelines confirmed the notion that explicit denomination of specific human rights duties in voluntary guidance is likely to suggest greater positive impact. While voluntary due diligence mechanisms do not create new law, it is evident that if explicitly named in due diligence documents, corporate ignorance of human rights duties can have legal consequences, hence making companies more aware of the need to respect human rights (Lindsay et al. (2013)).

Reporting requirements (option 3) likewise raise awareness among both companies and stakeholders and provide leverage for rights-holders to demand information. However, transparency and compliance are challenging to monitor and enforce (especially if contracting in the informal sector) as companies may perceive reporting and disclosure activities as procedural rather than substantive.

While very few (0% to 5%) respondents expected a negative impact, rather than a positive or neutral impact from reporting requirements, the literature suggests that such requirements might not have any impact on companies that already understand the value of transparent reporting for their consumer base. Impacts will instead focus most on those companies that do not willingly report. As such, reporting requirements risks missing an opportunity for rights-holders to demand their rights if transparency mechanisms are not enforced.

Finally, the evidence above regarding mandatory due diligence requirements as a legal duty of care (option 4) suggests that as long as robust risk assessment (based on the risks to those affected), transparency, monitoring, and compliance systems are enforced, and if the mechanism is designed to avoid unintended consequences, such as through wide standardisation to avoid circumvention, rights-holders can expect opportunities for protection. Regulation requiring mandatory due diligence allows for significant preventative benefits that reporting requirements fail to capture because of their retrospective nature. Due diligence requirements are especially likely to create substantive impact when they include demands for collaboration with external stakeholders and prioritize robust compliance mechanisms.

As explained in section 3.2.2, the regulatory options considered in this study imply that the legal obligations of companies gradually increase as we move from the new voluntary guidelines to mandatory due diligence. Table 8.61 summarizes the perceptions of stakeholders and companies, indicating whether the proportion is higher, lower, or the same compared to the previous regulatory option. Notably, among those who expect impacts, both, general stakeholders' and companies' perception that due diligence options would have a positive impact on specific human rights, increased for every fundamental right when moving from reporting requirements to mandatory due diligence as a legal duty of care. Interestingly, stakeholder perceptions that due diligence options would provide positive human rights impacts increased more than 10% for each duty when moving from option 3 to option 4. Companies likewise all increased expectations for positive human rights impacts when moving from option 3 to option 4 but increases of more than 10% were specifically evident for the Right to Non-Discrimination/Equality, and Women's Rights.

Interestingly, the amount of stakeholders that foresaw due diligence options to have positive human rights impacts decreased for five specific human rights when moving from voluntary guidelines to reporting requirements—these included the Right to Life, Liberty, and Security of Person; the Right to Physical and Mental Health; the Right to not be subject to Torture; Rights of the Child; and the Rights of Peoples with Disabilities. Companies felt that even more specific human rights, 10 to be specific, would not benefit by moving from voluntary guidelines to reporting requirements—these included the Right to Life, Liberty, and Security of Person; the Right to Physical and Mental Health; the Right to Freedom of Expression; the Right to Non-Discrimination/Equality; the Right to own Property; Right to Privacy; Right to Peaceful Assembly; Women's Rights; Rights of Indigenous Persons; and Rights of People with Disabilities. Results seem to suggest that both stakeholders and companies foresee mandatory due diligence as a legal duty of care to be more likely to have positive human rights impacts than any other mechanism. However, when comparing voluntary guidelines to reporting requirements, it seems all respondents foresee voluntary guidelines to be more effective of the two (options 2 and 3). The conclusion would thus be for regulation to either remain at voluntary guidelines level, or to fully implement mandatory due diligence, as reporting requirements seem to be perceived as ineffective in comparison.

The regulatory options considered in this study imply that the legal obligations of companies gradually increase as we move from the new voluntary guidelines to mandatory due diligence. The following table summarizes the perceptions of stakeholders and companies, indicating whether the proportion is higher, lower, or the same compared to the previous regulatory option. Two arrows indicate differences of more than 10%.

Stakeholders	Businesses

Table 8.61: Summary of respondents' perceptions about human rights impacts by area

	Negative		Neutral		Positive		No opinion/Do not know		Negative		Neutral		Positive		No opinion/Do not know	
	O2 to O3	O3 to O4	O2 to O3	O3 to O4	O2 to O3	O3 to O4	O2 to O3	O3 to O4	O2 to O3	O3 to O4	O2 to O3	O3 to O4	O2 to O3	O3 to O4	O2 to O3	O3 to O4
Right to Life, Liberty and Security of Person	↓	↑	↑	↓↓	↓↓	↑↑	↑	↓	↓	↓	↑	↓	↓	↑	↑	↓
Right to Physical / Mental Health	↓	↑	↑	↓↓	↓	↑↑	↑	↓	↓	↓	↑	↓	↓	↑	↑	↑
Right to not be subject to Torture	↓	↑	↑	↓↓	↓↓	↑↑	↑	↓	↓	↓	↓	↓	↑	↑	↑	↑
Right to Freedom of Opinion/Expression	↓	↓	↓	↓↓	↑	↑↑	↑	↓	↑	↓	↓	↓	↓	↑	↑	↑
Right to Non-Discrimination / Equality	↓	↑	↓	↓↓	↑	↑↑	↑	↓	↑	↓	↑	↓	↓↓	↑↑	↑	↑
Right to own Property	↓	↓	↓	↓↓	↑	↑↑	↑	↓↓	↑	↓	↓	↓	↓	↑	↑	↑
Right to freedom from Slavery	↓	↑	↓	↓↓	↑	↑↑	↑	↓	↓	↓	↓	↓	↑	↑	↑	↓
Right to Freedom from Arbitrary Arrest	↓	↓	↓	↓↓	↑	↑↑	↑	↓↓	↓	↓	↓	↓	↑	↑	↑	↑
Right to Privacy	↓	↑	↓	↓↓	↑	↑↑	↑	↓	↓	↓	↑↑	↓↓	↓↓	↑	↑	↑
Right to Peaceful Assembly / Association	↓	↑	↓	↓↓	↑↑	↑↑	↓	↓	↓	↓	↑	↓↓	↓	↑	↑	↑
Right to Education	↓	↓	↓	↓↓	↑	↑↑	↑	↓	↓	↑	↓	↓	↑	↑	↑	↑
Rights of the Child	↓	↑	↓	↓↓	↓	↑↑	↑	↓	↓	↑	↓	↓	↑	↑	↑	↑
Women's Rights	↓	↓	↓	↓↓	↑	↑↑	↑	↓	↓	↑	↑	↓↓	↓	↑↑	↑	↓
Rights of Indigenous Persons	↓	↓	↓	↓↓	↑	↑↑	↑	↓	↓	↓	↓	↓	↓	↑	↑	↓
Rights of People with Disabilities	↓	↑	↑	↓↓	↓	↑↑	↑	↓	↓	↓	↑	↓	↓	↑	↑	↑

- **Environmental Impacts**

shows that the more substantial differences in expected positive environmental effects are among stakeholders when moving from the new regulation requiring due diligence reporting (Option 3) to the new regulation requiring mandatory due diligence (Option 4). Also, neutral impacts and no opinion responses tend to decrease within this group, favouring the positive impacts category for all the areas. In the case of companies, the tendency is similar to stakeholders, but the change from one regulation option to the other does not bring forward differences of more than 10%. This means that companies' perceptions are more spread across categories, and as indicated in the detailed results, they often prefer the 'no opinion/do not know' answer. Overall, the table clearly shows that for both stakeholders and companies, the expectations of positive impacts across all areas increases when moving from Option 3 to Option 4.

	Stakeholders								Businesses							
	Negative		Neutral		Positive		No opinion/Do not know		Negative		Neutral		Positive		No opinion/Do not know	
	O2 to O3	O3 to O4	O2 to O3	O3 to O4	O2 to O3	O3 to O4	O2 to O3	O3 to O4	O2 to O3	O3 to O4	O2 to O3	O3 to O4	O2 to O3	O3 to O4	O2 to O3	O3 to O4
Environmental Air Pollution	=	↑	↑	↓↓	↓	↑↑	↑	↓	↓	↓	↑	↓↓	↑	↑	↑	↑
Waste	=	↑	↑	↓↓	↑	↑↑	↑	↓	↓	↓	↓	↓↓	↑	↑	↓	↑
Energy use and mix	=	↑	↓↓	↓↓	↑	↑↑	↑	↓	↓	↓	↓	↓	↑	↑	↓	↑
Transport	=	=	↑	↓↓	↓↓	↑↑	↑↑	↓	↑	↓	↓	↓↓	↑	↑	↓	↑
Water Resources	=	=	↑	↓↓	↓↓	↑↑	↑	↓↓	↑	↓	↓	↓	↑	↑	↑	↑
Biodiversity	↓	↓	↓	↓↓	↓	↑↑	↑	↓	↓	↓	↓	↓	↑	↑	↓	↓
Agricultural Fertilisers	↓	↓	↓	↓↓	↓	↑↑	↑	↓↓	↑	↓	↑	↓	↓	↑	↓	↓
Forests	↓	↓	↓	↓↓	↓	↑↑	↑	↓↓	↑	↓	↓	↓	↑	↑↑	↑	↓

Fisheries	↑	↓	↓	↓↓	↓	↑↑	↑	↓↓	↑	↓	↓	↓	↑	↑	↓	↑
Greening of the Economy	↓	↓	↓	↓↓	↓	↑↑	↑	↓↓	↑	↓	↓	↓	↑	↑	↓	↑

Table 8.62: Summary of respondents' perceptions about environmental impacts by area

- **Impacts on Public Authorities**

For the options 2 and 3 it is expected that the costs would remain limited as these would mainly require the drafting of new guidelines, the provision of guidance on their implementation and possibly sample reviews and the creation and maintenance of a database for the company reports (for option 3).

The additional costs for the monitoring of the implementation of the regulation under option 4 are expected to be significant, especially if enforcement is to take place at Member State or EU level (sub-option 4.3(b)). Legal sanctions or liability for failure to comply would be necessary if the objective was that sub-options 4.1 and 4.2 would be mandatory.

The costs for monitoring and coordination under option 4 are expected to increase with the number of affected companies since this would require more compliance controls and inspections and as a result more personnel at the European Commission as well as more personnel in each Member State. In addition, the sub-option of 4.3(b) is expected to imply significant additional costs for the state-based oversight mechanism in EU Member States, depending on the chosen oversight and enforcement mechanism. By comparison, judicial remedies as foreseen in sub-option 4.3(a) are likely to have significantly less additional costs for Member States, insofar as these costs would fall within existing budgets for courts and the judicial system.

4. Global Comparison of Regulatory Options

This section provides a succinct conclusion for expected impacts under each policy scenario. A comprehensive and detailed analysis is provided above in section 3, and a broader overview below in Table 4.1.

Option 1: No policy change

For option 1, most impacts depend on the development of national initiatives. No impact on employment levels is expected. The impacts for public authorities depend also on the national developments. Diverging national legal developments may create monitoring and coordination cost for EU bodies.

Human rights, social, and environmental impacts likewise depend on the development of national initiatives under policy option 1. However, while expectations regarding direct human rights impacts cannot be formed under no policy change, given the nature of depleting environmental resources, it is expected that no policy change might result in negative environmental impacts.

Option 2: New voluntary guidelines/guidance

Some costs could arise for public authorities from the creation and promotion of new guidelines, but these are expected to remain relatively small.

Option 2 is expected to have very small or no social impacts. Voluntary guidelines can be expected to provide some benefits for regarding human rights as well as the environment by raising awareness, as well as increasing transparency and corporate accountability. However, positive impacts are risked being ineffective as they lack enforcement mechanisms and are dependent on company willingness to comply and transparently share procedural details. Additionally, voluntary guidelines run an additional risk of being exploited by companies that advertise to be in line with guidance but take no steps to implement.

Specific to environmental impacts, voluntary guidelines are exceptionally difficult to compare across national borders as companies may find themselves on unequal grounding for compliance. Country and capacity context may make it difficult to commit to compliance as well as monitoring to reduce emissions/potential harms to the environment. While vigilance plans may be insufficient to address adverse impacts, operational costs and lack of capacity may act as compliance barriers.

Option 3: New regulation requiring due diligence reporting

Costs for public authorities are expected to be higher as the monitoring of implementation would require more personnel. Additional costs may arise from the provision of guidance on implementation, sample reviews of reports and possibly the creation and maintenance of a database for the company reports. Regarding firm-level costs for the EU28, if new regulation would be applied horizontally across the EU, "New reporting requirements" would cause additional aggregate cost of about 3.5 billion EUR annually.

Option 3 could potentially have small impacts on work conditions and labour rights. No impact on employment levels is expected. Option 3 can be expected to provide positive impacts for rights-holders. Even if full transparency is challenging, reporting requirements raise awareness among both companies and stakeholders and provide leverage for rights-holders to demand information.

In regard to environmental protection, *reporting requirements would be estimated to result in positive impacts as companies will have a mandate to investigate and e*nhance their identification of existing and potential adverse environmental impacts. This will increase visibility and transparency of climate-related due diligence both within the company as well as externally.

However, in regard to both human rights and environmental impacts, positive impacts are dependent on proper monitoring and enforcement mechanisms as companies may perceive reporting and disclosure activities as procedural rather than substantive. Difficulties in monitoring disclosure activities for the informal sector are particularly challenging.

Option 4: New regulation requiring mandatory due diligence as a legal duty of care

Any type of enforcement mechanism under option 4 could potentially imply considerable costs for public authorities. It is expected that any costs for monitoring the implementation would increase with the number of affected companies as any compliance controls and inspections would require more personnel. Especially, sub-option of 4.3(b) is expected to imply significant additional costs for the state-based oversight mechanism in EU Member States, which depend on the chosen oversight and enforcement mechanism.

Firm-level costs specific to new regulation requiring mandatory due diligence as a legal duty of care limited by sector to a narrow category of business vary. Total additional cost for EU companies operating in the mining and extraction industries to amount to up to EUR 42.3 million EUR (EUR 6.2 million EUR for large companies and EUR 36 million EUR for SMEs). The total additional cost for EU companies operating in the textiles industries are estimated to amount up to EUR 110 million per year (EUR 3.7 million for large companies and EUR 107 million for SMEs). The total additional cost for EU companies that trade, or manufacture food products and agricultural commodities amount to up to EUR 2.3 billion annually (EUR 56 million for large companies and EUR 2.27 billion for SMEs).

In regard to "Mandatory DD throughout companies' value chains", (sub-option 4.2(a), large companies' additional annual cost amount to about 543 million EUR. If new regulation would be applied horizontally across the EU applying to all businesses (sub-option 4.2(b), EU companies' additional cost would amount to about 33 billion EUR annually. Large companies' additional annual cost amount to about 543 million EUR. SMEs' additional annual cost amount to about 32.5 billion EUR.

Option 4 could also provide significant economic benefits for firms related to their brand image, reputation and sales, if companies will, as a result of the new regulation, increasingly implement due diligence activities and these are known by consumers. Similarly, economic benefits in the area of human resources can be expected as sustainability measures and CSR activities can make a company more attractive for job applicants and therefore companies can attract talents even when they do not pay highly competitive salaries. Economic benefits can also be expected from better risk management, operational efficiency and innovation. Several studies have found that sustainability measures by firms have a positive impact on the company risk and operational efficiency which translates into economic value. It can also be expected that economic benefits for companies arise in the form of better financial or stock performance and access to lower cost of capital if a new EU regulation requires mandatory due diligence and leads to improved due diligence measures taken by companies. Several studies find a positive relationship between companies' sustainability activities and financial or stock performance. Other studies also suggest that sustainability activities of companies can have a positive impact on companies' cost of capital.

However, social, human rights, and environmental impacts from option 4 are expected to be most significant. In fact, while this study is not scoped around the assessment of the effectiveness of mandatory due diligence on achieving the SDGs, it is notable that the improvement of the socio-economic-environment situation in countries hosting EU company suppliers could have an inherent effect towards achieving the SDGs.

The magnitude of the social impacts depends on the application of the new regulation (the more companies affected, the higher the expected negative and positive impacts), the social issues which are expected to be addressed and specified by the regulation and thus to be covered by companies, and the effectiveness of an enforcement mechanism to ensure the implementation of due diligence practices.

Regulation requiring mandatory due diligence allows for significant preventative benefits for rights-holders that reporting requirements fail to capture because of their retrospective nature. Additionally, sector-specific due diligence is expected to have even more significant impacts as requirements may dive deeper and be designed to be more context-specific towards the needs of specifically impacted stakeholders. However, even when due diligence is mandatory, compliance is challenging to monitor and enforce. Challenges likewise arise from over-reliance on certification schemes when investigating suppliers beyond a company's direct supplier. And finally, when it comes to sector-specific mandatory due diligence, there is a risk of unintended consequences such as de-facto embargoes of certain local and developing economies that depend on the demand of a sector-specific product for their livelihood.

Concerning environmental impacts, a common due diligence framework may ease and improve compliance along supply/value chains. Mandatory requirements likewise provide higher accountability, and enhanced access to justice in case of adverse environmental impacts. Arriving at consensus regarding positive impacts across various environmental areas may indicate receptivity to adopt new approaches to environmental/ climate-change impact mitigation. However, positive environmental impacts are dependent on institutional capacities to implement and properly enforce such frameworks. Additionally, stringent regulations under policy option 4 must be weary not to tip the scale and incentivize infrastructure development for regulatory evasion (e.g. sourcing from countries with significantly less stringent regulations compared to the UN Guiding Principles or the OECD Guidelines, for instance).

Table 8.63: Overview of regulatory options and impacts by area

	Economic Impacts	Social Impacts	Impacts on Human Rights	Environmental Impacts	Impacts on Public Authorities
Option 1: No policy change	*Company-level costs* • No changes *Company-level benefits* • Economic benefit expected only if companies advance due diligence activities on their own behalf and succeed to communicate these. Then economic benefits can accrue for brand image and reputation, human resources, risk management and operational efficiency, as well as stock/financial performance or capital cost.	*Benefits* • Impacts on work conditions and labour rights depend on the development of national initiatives. • No impact on employment levels expected.	*Benefits* • Existing guidelines have successfully began transitioning due diligence from retrospective expressions of regret to proactive monitoring and investigation. *Challenges* • As the current landscape is dominated by guidelines and voluntary mechanisms, companies are not held accountable for respecting human rights duties. • Gaps in legal certainty with multiple standards in various Member States, third countries and industries, ranging from non-binding to binding, issue-specific to general, and industry-specific to cross-sectoral. This leaves companies with lack of clarity and rights-holders with lack of access to remedy.	*Challenges* • Unclear link between environmental and climate-related due diligence; the latter is considered as a sub-aspect of environmental due diligence rather than an explicit priority. • Increasing number of disputes and arbitration cases between governments and companies derived from infringement of regulations or the increment of environmental protection.	*Costs* • Initiatives at national level and cost for national authorities are difficult to predict. • Possible monitoring and coordination cost for EU bodies could arise.

	Economic Impacts	Social Impacts	Impacts on Human Rights	Environmental Impacts	Impacts on Public Authorities
Option 2: New voluntary guidelines/guidance	*Company-level costs* • No significant changes *Company-level benefits* • No economic benefits expected, unless (like under Option 1), companies pursue due diligence practices voluntarily or due to national requirements.	*Benefits* Very small or no impact expected on work conditions and labour rights unless companies take voluntary actions. No impact on employment levels expected.	*Benefits* • Voluntary guidelines raise awareness and provide rights-holders with a benchmark against which to hold companies accountable. *Challenges* • Voluntary guidelines risk being exploited by companies that advertise to be in line with guidance but take no steps to implement. • Voluntary guidelines lack enforcement mechanism and rely on a company's willingness to respect human rights.	*Challenges* • Unequal situation for companies (and countries) regarding their commitment to reduce emissions/potential harms to environment. • Companies' vigilance plans potentially insufficient to address adverse impacts. Increased operation costs deter larger efforts.	*Costs* • Possible personnel costs could arise for the promotion of new guidelines throughout the EU (0.05 FTE).[1497]

[1497] A "full-time equivalent" (FTE) is equivalent to one employed person working on a full-time schedule.

	Economic Impacts	Social Impacts	Impacts on Human Rights	Environmental Impacts	Impacts on Public Authorities
Option 3: New regulation requiring due diligence reporting	*Company-level costs* • Total of additional annual internal labour cost for EU28: EUR 2.44 billion EUR. • Total annual cost incl. labour cost, overhead and costs of outsourced activities / audits for EU28: EUR 3.5 billion. *Company-level benefits* • Similar to Option 2, economic benefits depend on the extent to which mandatory reporting requirements enact changes in companies' policies and promote the taking of actions.	*Benefits* • Small impacts on work conditions and labour rights possible if mandatory reporting requirements lead to improvements in due diligence practices and company policies. • No impact on employment levels expected.	*Benefits* • Even if full transparency is challenging, reporting requirements raise awareness among both companies and stakeholders and provide leverage for rights-holders to demand information. *Challenges* • Compliance with reporting requirements is challenging to monitor and enforce. • Companies may perceive reporting and disclosure activities as procedural rather than substantive. • Difficulties in monitoring disclosure activities for the informal sector.	*Opportunities* • Enhanced identification/ assessment of existing/potential adverse environmental impacts within companies. • Increased visibility and transparency of climate-related due diligence. • Common environmental due diligence framework for companies to understand what is expected of them. *Challenges* • High uncertainty about impacts in specific areas (eg transport). • Low levels of enforcement /lack of sanctions for non-compliance, legal liability or access to remedy.	*Costs* • The creation and maintenance of a database for company reports could create additional costs (5 FTEs).

	Economic Impacts	Social Impacts	Impacts on Human Rights	Environmental Impacts	Impacts on Public Authorities
Option 4: New regulation requiring mandatory due diligence	*Company-level benefits* • Expected benefits depend on the coverage of companies and enforceability of required due diligence measures as described for sub-options.	*Benefits/Costs* • Social impacts are expected to be highest if mandatory due diligence is required. • There could be negative (if the economic burden for companies is high) as well as positive impacts on employment levels (resulting from an increased demand for specialised staff).	*Benefits* • Regulation requiring mandatory due diligence allows for significant preventative benefits that reporting requirements fail to capture because of their retrospective nature. *Challenges* • Even when due diligence is mandatory, compliance is challenging to monitor and enforce. • There are currently few cases of due diligence requirements to provide comparative information about potential impacts. • Reliance on certification schemes when investigating suppliers beyond a company's direct supplier.	*Opportunities* • Common environmental due diligence framework may ease and improve compliance along supply/value chains. • Enhanced accountability and access to justice in case of adverse environmental impacts. • Consensus about positive impacts across various environmental areas may indicate receptivity to adopt new approaches to environmental/ climate-change impact mitigation. *Challenges* • Institutional capacities to implement/enforce environmental due diligence may be limited. • Stringent environmental regulations may increase avoiding compliance (e.g. relocation to "pollution havens").[1498]	*Costs* Same costs expected as for Option 3 plus additional costs as described per sub-option.

[1498] Candau, Fabien, and Elisa Dienesch. 2017. "Pollution Haven and Corruption Paradise". *Journal of Environmental Economics and Management* 85: 171-192. doi:10.1016/j.jeem.2017.05.005.

	Economic Impacts	Social Impacts	Impacts on Human Rights	Environmental Impacts	Impacts on Public Authorities
Sub-option 4.1: Narrow category of business (limited by sector)	*Company-level costs* • Total additional cost for EU companies operating in the mining and extraction industries to amount to up to EUR 42.3 million EUR (EUR 6.2 million EUR for large companies and EUR 36 million EUR for SMEs). • The total additional cost for EU companies operating in the textiles industries are estimated to amount up to EUR 110 million per year (EUR 3.7 million for large companies and EUR 107 million for SMEs). • The total additional cost for EU companies that trade or manufacture of food products and agricultural commodities amount to up to EUR 2.3 billion annually (EUR 56 million for large companies and EUR 2.27 billion for SMEs). *Company-level benefits* • For individual companies benefits from an enhanced reputation and for human resources are expected to be rather small, but potential significant benefits associated with reduction of reputational risks associated with current status quo. • Economic benefits for risk management, operational efficiency and innovation as well as financial/stock performance are expected to remain same as for Option 4 generally.	*Benefits/Costs* • Social impacts depend on the size/number of sectors to which the regulation will be applicable: the larger the number of companies affected, the higher the potential benefits for work conditions and labour rights. • Similarly, the higher the number of affected companies, the higher is potentially the number of additional jobs created in CSR. However, possible negative effects can also be higher if a resulting significant economic burden leads to reduced production and lower demand for labour in many companies.	*Benefits* • Rights-holders benefits may be seen more significantly as requirements may dive deeper and be more specific. *Challenges* • However, there is a risk of unintended consequences such as de-facto embargoes of certain local and developing economies that depend on the demand of a sector-specific product for livelihood.	See sub-section on environmental impacts	*Costs* • Costs would arise for personnel at Member State level in designated control bodies (estimated at 1.5-2 FTE per MS).

	Economic Impacts	Social Impacts	Impacts on Human Rights	Environmental Impacts	Impacts on Public Authorities
Sub-option 4.2: Horizontally across sectors	*Company-level costs* • If new regulation would be applied horizontally across the EU, EU companies' additional cost would be highest for Option 4, amounting to about EUR 33 billion annually. *Company-level benefits* • Expected benefits depend on the coverage of companies as described below.	*Benefits/Costs* • Social impacts depend on the coverage of affected companies as discussed for sub-option 4.1.	See sub-section on human rights impacts	See sub-section on environmental impacts	*Costs* • Cost to set up structures and processes to monitor the implementation are expected to be similar as for Option 4.1 • Expected operating costs for sub-options 4.2(a) to 4.2(c) will depend on the number of affected companies.

	Economic Impacts	Social Impacts	Impacts on Human Rights	Environmental Impacts	Impacts on Public Authorities
Sub-option 4.2(a): Set of large companies	*Company-level costs* • Large companies' additional cost would be highest for Option 4, amounting to about EUR 543 million. *Company-level benefits* • The extent of economic benefits from enhanced brand image and reputation and human resources depends on the number of affected companies: The fewer companies are affected, the more likely are reputational and human resource-related benefits for the individual company. • Potential benefits associated with reduction in reputational risks present in current status quo.	*Benefits/Costs* • Less social benefits are expected for work conditions and labour rights expected than for sub-option 4.2(b) since this option applies to a smaller subset of companies (see also explanations for sub-option 4.1). Similarly, possible positive and negative employment impacts are expected to be lower than for sub-option 4.2(b).	See sub-section on human rights impacts	See sub-section on environmental impacts	*Costs* • The potential costs depend on the number of affected companies (large companies account only for 1% of EU companies).[1499]

[1499] Eurostat (2018). Statistics on small and medium-sized enterprises. Available at: https://ec.europa.eu/eurostat/statistics-explained/index.php/Statistics_on_small_and_medium-sized_enterprises.

	Economic Impacts	Social Impacts	Impacts on Human Rights	Environmental Impacts	Impacts on Public Authorities
Sub-option 4.2(b): All business, including SMEs	*Company-level costs* • If new regulation would be applied horizontally across the EU, EU companies' additional cost would be highest for Option 4 requiring, amounting to about EUR 33 billion annually. *Company-level benefits* • Benefits may be lower if the regulation is applied EU-wide as individual companies lose their competitive advantage from reputational effects vis-à-vis other companies. • Risk management, operational efficiency and stock/financial performance benefits are expected to remain the same as generally for option 4.	*Benefits/Costs* • It is expected that positive impacts for work conditions and labour rights would be highest if due diligence requirements apply to all companies. • Similarly, positive and negative impacts on employment levels are expected to be most significant if due diligence requirements apply to all companies.	See sub-section on human rights impacts.	See sub-section on environmental impacts.	*Costs* • It is expected that this option will create higher costs than sub-option 4.1 as it applies to more companies. • The costs for setting up structures and processes are expected to be similar as for sub-option 4.1, but the operating costs for monitoring and coordination are expected to increase with the number of affected companies.

	Economic Impacts	Social Impacts	Impacts on Human Rights	Environmental Impacts	Impacts on Public Authorities
Sub-option 4.2(c): All business plus specific additional obligations only applying to large companies		*Benefits/Costs* • This option could increase impacts on work conditions and labour rights compared to options 4.1, 4.2(a) and 4.2(b) depending on the specification of the additional obligations. • It could also increase impacts (positive and negative) on employment levels since large companies would be subject to increased due diligence requirements (leading to more labour demand in CSR) but also a potentially higher economic burden from compliance.	See sub-section on human rights impacts	See sub-section on environmental impacts	*Costs* • The cost of monitoring additional obligations depends on the type of obligations and the resulting requirements for additional staff and/or additional processes and structures.
Sub-option 4.3: Statutory oversight and/or enforcement	*Company-level benefits* • Enforcement mechanisms are expected to increase compliance and as a result credibility of companies' due diligence activities. This could potentially increase economic benefits in all discussed areas.	*Benefits/Costs* • An enforcement mechanism could increase companies' compliance and the likelihood that the expected social impacts come into effect.	See sub-section on human rights impacts	See sub-section on environmental impacts	*Costs* • This option could create significant additional costs for public authorities and the legal systems in EU Member States, depending on the design of the enforcement method.

	Economic Impacts	Social Impacts	Impacts on Human Rights	Environmental Impacts	Impacts on Public Authorities
Sub-option 4.3(a): Mechanisms for judicial or non-judicial remedies	See discussion under sub-options	See sub-section on social impacts	See sub-section on human rights impacts	See sub-section on environmental impacts	*Costs* • The additional cost of this option depends on whether existing judicial or non-judicial structures can be used or new bodies and/or processes need to be established.

	Economic Impacts	Social Impacts	Impacts on Human Rights	Environmental Impacts	Impacts on Public Authorities
Sub-option 4.3(b): State-based oversight body and sanction for non-compliance	See discussion in sub-section	See sub-section on social impacts	See sub-section on human rights impacts	See sub-section on environmental impacts	*Costs for public authorities* • Costs for a new body expected to be higher compared to financing additional staff within existing institutions. • Additional costs expected for training and expert staff. • An oversight and enforcement body in each EU Member State would imply significant additional costs. • Income through fines paid to public authorities may cancel out costs.

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