Corporate sustainability due diligence


This briefing provides an initial analysis of strengths and weaknesses of the European Commission’s impact assessment (IA) accompanying the above-mentioned proposal, submitted on 23 February 2022 and referred to the Parliament’s Committee on Legal Affairs (JURI). This initiative is in the 2021 Commission work programme and Joint Declaration on EU 2022 legislative priorities.1

The transition to sustainability is embedded in EU political priorities and the objectives of becoming climate-neutral by 2050 and delivering on the United Nations Sustainable Development Goals. Businesses and their directors can contribute to a more sustainable economy and fair society, by considering the risks of adverse impacts on the environment and on human rights in their decisions.

This proposal responds to two Parliament resolutions in 2020 and 2021, and to Council conclusions calling on the Commission to present a proposal for an EU legal framework on sustainable corporate governance, including corporate due diligence along global value chains. Sustainable corporate governance was so far mostly promoted indirectly at EU level, by imposing reporting requirements through the Non-Financial Reporting Directive (NFRD), and the proposed corporate sustainability reporting directive (CSRD, revision of NFRD),2 and by providing a categorisation of environmentally sustainable economic activities with the Taxonomy Regulation to facilitate sustainable investment.

This initiative was initially referred to as sustainable corporate governance,3 which encompasses decision-making structures, management processes and allocation of competences within a company. After a delay, the legislation was proposed under the title of corporate sustainability due diligence, which focuses on the identification, prevention and mitigation by a company of actual and potential adverse impacts on human rights and the environment, in its actions and value chains.

This proposal is accompanied by a communication on decent work worldwide, as part of the ‘just and sustainable economy’ package. It would complement EU environmental, climate and human rights legislation, as well as EU instruments on supply chain due diligence applying to specific products.4 It would also contribute to the objectives of the global EU response to COVID-19.

Following two successive negative opinions from the Commission Regulatory Scrutiny Board (RSB), a follow-up document accompanying the proposal was prepared to complement the IA (see section on ‘Follow-up to the opinion’). In addition, the content and scope of application of the IA’s preferred options were revised by the Commission in its proposal, as a response to RSB criticism (for more details, see section on ‘Coherence with the Commission proposal’).

Problem definition

According to the IA, the main problem is that ‘sustainability is not sufficiently integrated in corporate governance’ (IA, pp. 7-16). It can be split into two ‘sub-problems’, which correspond to the two dimensions of sustainable corporate governance:

1 Stakeholder-related (sustainability) risks to the company and opportunities are not sufficiently addressed in the best interest of the company (the internal dimension);
Companies fail to sufficiently address adverse impacts on people and the environment in their own operations and value chains in line with the EU’s international environmental and human rights commitments (the external dimension).

The problem drivers identified by the IA (IA, pp. 16-29) are a combination of market failures (e.g. a short-term focus among companies and investors) and regulatory inefficiencies (e.g. unclear and diverging national laws). These causes of the problem are illustrated in the IA (p. 7), as well as its consequences for the various stakeholders: the company, its employees, investors, long-term shareholders, as well as consumers, the economy, society, the environment and third countries.

The IA also explains how the problem is likely to evolve without EU action (IA, pp. 30-31) resulting in ‘sub-optimal levels of corporate investments into longer term (innovative) projects’, outsourced ‘activities in third countries with mostly lower human rights and environmental standards’ and increased fragmentation due to Member States setting up rules in the absence of EU legislation.

Overall, the problem definition (IA, pp. 7-30), is detailed and substantiated with economic theoretical literature and research reports, in particular the two supporting studies (see section on ‘Supporting data’), as well as with some contributions from the public consultation. Annex 10 provides additional evidence and examples (IA, part 2, pp. 157-164), which contributes to illustrate the scope of the problem. The problem definition is complemented by the follow-up document (pp. 1-6), showing progress in the uptake of sustainability practices, which remains slow in some areas.

**Subsidiarity / proportionality**

This initiative is based on Article 50 of the Treaty on the Functioning of the European Union (TFEU), which is a legal basis for company law legislation for the protection of the interests of companies’ members and others, and Article 114, which is the legal basis for proper functioning of the internal market. The proposed instrument is a directive, as required by Article 50.

A subsidiarity grid accompanies the IA, as recommended by the Task Force on Subsidiarity, Proportionality and ‘Doing Less More Efficiently’. The problem cannot be tackled effectively at national level, because of its trans-boundary nature and the increasingly global nature of value chains (IA, pp. 30-32). The IA thus justifies the need for and value added by EU action, as it would improve legal certainty and level the playing field for companies in the single market. Under the subsidiarity control mechanism, the Swedish Parliament submitted a reasoned opinion before the 25 May 2022 deadline, arguing that some issues would be best managed at national level.

**Objectives of the initiative**

The general objective as set in the IA is ‘to better exploit the potential of the single market to contribute to the transition to a sustainable economy, to foster sustainable value creation and improve the long-term performance and resilience of EU companies. These objectives will be achieved through: (1) increasing directors’ accountability for sustainable value creation and incorporating (long-term) sustainability factors in decision-making of companies; and (2) increasing corporate responsibility for preventing and mitigating adverse human rights and environmental impacts, including in companies’ value chains, in line with the EU’s international commitments regarding human rights and the environment’. This general objective translates into five specific objectives (IA, pp. 32-33, emphasis added):

- clarify what is expected of directors in order to fulfil their duty to act in the company’s interest as regards stakeholder interests and the long-term interests of the company;
- foster the integration of sustainability risks (including from the value chain) and impacts into corporate risk management processes, impact mitigation processes, strategies, facilitate management of dependencies and ability to react to change;
- increase accountability for identifying, preventing and mitigating adverse impacts, including in value chains;
- improve access to remedy for those affected by adverse impacts;
improve corporate governance practices to facilitate the integration of sustainability into directors' and company decision-making (e.g. stakeholder involvement).

It is of note that in the proposal, only parts of the general objectives (in bold above) have been retained (p. 45), while specific objectives were revised (p. 3), suppressing parts related to directors' duties. According to the follow-up document, ‘the legislative proposal now focuses on external impact mitigation through value chain due diligence’ (one dimension of the problem), and only covers directors’ duties necessary for the proper implementation of due diligence (IA, p. 42, p. 45).

Overall, the objectives are neither entirely measurable nor time-bound, and thus do not comply fully with the ‘S.M.A.R.T.’ criteria (BRG, Tool #16). The IA also fails to identify operational objectives defining deliverables of policy actions under the preferred options (BRG, Tool #16). This would have contributed to defining targets, and facilitating later evaluation of the success of this initiative.

Range of options considered

The IA describes clearly what would happen in the baseline scenario (IA, p. 33-38), as well as other European and national actions. In the follow-up to the RSB’s second opinion (SWD(2022) 39, pp. 1-6), additional evidence was provided to make the description of the baseline scenario more dynamic, in particular through better consideration of the increasing uptake of sustainability practices.

The IA identifies policy options across three main areas: corporate due diligence, directors’ duties and their remuneration. In the first two areas, the IA retained four options in addition to the baseline, with some elements that are common to several or even all options (e.g. regarding enforcement of the due diligence obligation). On directors’ remuneration, only one option was considered, which is not in line with the BRG (Tool #17). Table 1 below shows the respective baseline and policy options considered in the IA for each area, as well as its preferred options (highlighted in blue). Elements of the preferred options that differ between the IA and the proposal are in italics.

The content of the policy options is set out clearly (IA, pp. 38-50, Annex 13, pp. 184-191). The IA explains why some options were discarded at an early stage. In particular, non-regulatory options (e.g. recommendation, guidelines, and training) were excluded due to their limited effectiveness.

For due diligence (DD), potential options were screened along three criteria: 1) personal scope, i.e. companies to which the obligations apply – DD requirements cover limited liability companies (LLC), options and regime vary in terms of company size and sector (full versus more targeted or simplified due diligence obligation); 2) material scope, i.e. content of the DD duty – options vary depending on sectors or impact categories covered (theme-specific, i.e. covering only selected impacts, or horizontal covering all sectors, human rights and environmental impacts) and the extent to which specific company categories have to fulfil the DD obligation; 3) enforcement, i.e. how to ensure that companies comply with obligations – all options include administrative enforcement by national authorities, civil liability, access to remedy (IA, pp. 38-46 and Annex 13).

The lists of adverse human rights and environmental impacts covered by the initiative (in annex to the proposal, parts I and II), are based on international human rights and environmental conventions listed in Annex 17 (IA, p. 44, part 2, pp. 215-217). The IA presents a methodology for selecting high-impact sectors (i.e. sectors where human rights and environmental adverse impacts are more likely to occur) and discusses possible lists, showing the total number of companies covered (IA, Annex 11, pp. 165-179). However, the range of high-impact sectors was limited in the proposal to sectors and parts of value chains covered by existing Organisation for Economic Co-operation and Development (OECD) due diligence guidance (see follow-up document, p. 11), resulting in a reduced number of high-impact midcap companies covered.

The definition of company sizes used in the IA are based on the Accounting Directive, but ‘only for listed companies and where the scope is aligned with that of the CSRD proposal’. Otherwise the IA uses ‘slightly amended (simplified) definitions for medium-sized and large companies’, based on the number of employees and the turnover, as proxies for their resources to properly conduct due
diligence and influence in the value chains. A category of 'midcaps' is used in the IA, 'to differentiate companies that exceed the medium-sized limits but are not very large' (IA, p. 42). The IA also introduces ‘additional categories of larger companies: three variants for defining very large companies and two middle-ground categories of large companies to differentiate midcaps from the very large companies’ (IA, part 2, p. 192).

This variation of definitions affects the number of companies falling in each group. In particular, the definitions for groups 1 and 2 were revised in the proposal compared to the IA’s preferred options (see endnotes in Table 1), which significantly impacted the number of companies falling under the scope of application of the DD duty (see section on ‘Small and medium-sized enterprises' (SMEs)).

Table 1 – Overview of the policy options considered in the IA

Assessment of impacts

For the assessment of possible impacts, the IA mostly relied on desk research (including the supporting studies), stakeholder consultations (IA, Annex 4, pp. 36-107) and examples from other countries which have due diligence in place (e.g. Germany, and the French Duty of Vigilance Law, ‘despite being too new to have already generated evidence-based insights regarding its impacts’). The assessment of impacts in Annex 4 focuses on economic impacts, essentially affecting companies, trade, investment, international competitiveness, and consumer prices (pp. 40-99). The other types of impacts are described in a less extensive way, even though they are particularly relevant in this initiative. Social impacts presented are mostly related to working conditions, employee satisfaction and health (pp. 100-101). The IA also shows the positive impacts expected on the protection of fundamental and human rights (pp. 102-104), as well as the anticipated reduction of adverse environmental impacts (pp. 104-107). In response to RSB criticism, the follow-up document contains additional information on the assessment of impacts (on competition, competitiveness and third countries), and a recalculation of the costs of the revised options (follow-up, p. 17-27). The summary table of benefits and costs was also revised (follow-up, pp. 35-40).

In the IA and the follow-up document, benefits are described in a qualitative way. Reduced adverse human rights and environmental impacts are expected to directly benefit employees of the company and its value chain partners, local communities, and actual and possible victims of such impacts, who will also benefit from improved access to justice. For companies (IA, part 2, pp. 40-49), the main benefit is increased competitiveness and financial performance expected from improved operational efficiency and cost savings, reputational gains, more attractiveness for talent and innovation, and first-mover benefits in global markets.

As the adopted proposal’s scope is significantly smaller than the IA’s preferred options (see section on ‘Coherence with the Commission proposal’), the costs for EU and non EU companies were recalculated in the follow-up document, using the same method as the IA (IA, part 2, pp. 49-93 and follow-up, pp. 17-18). The Commission estimates that the aggregated compliance costs implied for EU businesses (mainly the procedural costs to set up DD procedures), are reduced by more than half compared to IA estimations, down to €760 million recurrent and €220 million one-off costs, which is mainly driven by the exclusion of SMEs from the scope. As regards administrative (reporting) costs, ‘all companies covered under the new scope will already be required to disclose to the public sustainability and due diligence-related information’ under the CSRD. Therefore, no substantial additional administrative costs are expected for EU companies under this initiative, as reflected in the table on the ‘one-in-one-out’ approach10 (follow-up document, pp. 17-18 and Annex 2).

For due diligence and directors’ duties, the IA (pp. 50-88) compares options against the criteria of effectiveness (against the specific objectives), efficiency (cost-effectiveness), and coherence (IA, pp. 87-88), as recommended in the BRG (p. 28), and according to their respective costs (IA, pp. 56-60 and pp. 73-77). In addition, the IA provides an assessment of benefits and of proportionality.

However proportionality concerns were raised in the negative RSB opinions, leading the Commission to restrict the content and scope of the IA’s preferred options (follow-up, p. 43). The options as revised in the proposal are therefore considered more proportionate than those in the IA, as they allow ‘for reducing business’ compliance costs substantially and also for lowering the supervisory costs’ (follow-up, p. 20). The Commission considers that the revised options allow ‘still to decisively move forward towards the overall objective’ of the proposal (COM(2022) 71, p. 21). However, the follow-up document would also have benefited from analysis as to how the revised options are expected to be effective in achieving the objectives of the proposal.

SMEs / Competitiveness

An SME test was conducted (IA, Annex 5, pp. 108-116), following the steps described in Tool #22 of the BRG. For proportionality considerations, the IA excluded all micro-companies and non-listed small ones from the scope of options. Other SMEs are considered in two groups: listed non-micro
SMEs (already covered by DD reporting under the CSRD) and high-impact medium-sized companies. The most significant cost expected from this initiative concerns direct compliance costs (one-off and recurrent) related to the DD obligation. The IA also points to potential cost savings (tentatively quantified in the IA, Annex 4). The SME test highlights the indirect compliance costs to be incurred by supply chain companies, including SMEs not under the scope of the IA’s preferred options.

In the revised options, SMEs and smaller midcap companies, that ‘overall account for around 99% of all companies in the Union’ (COM(2022) 71, p.14), are fully excluded from the scope of the proposal, to better take account of possible constraints they may face to conduct DD (as outlined in a recent study). However, the proposal still includes larger midcap companies mainly active in one of the identified high-impact sectors (see endnote 13), for which the DD obligation will be simplified and application delayed, to alleviate their burden. SMEs involved in the upstream supply chains of larger companies, will be indirectly affected by DD. The proposal includes accompanying measures to support all companies, including SMEs, which may be indirectly affected.

The IA also analyses the potential impact of the initiative on EU companies’ competitiveness (IA, Annex 4, p. 86-89), complemented by additional information in response to the RSB’s comments (follow-up document, p. 25-27). Even if some uncertainty persists, the assessment suggests that the benefits from this initiative ‘are expected to outweigh its costs even at the corporate level, and will bring competitive advantages, at least in the medium to long-term’.

Simplification and other regulatory implications

Annex 7 to the IA lists all existing and planned EU legislation linked to this initiative, describing potential synergies and added value (IA, part 2, p. 120-150).

Impact on third countries and developing countries

The IA is quite succinct in its assessment of the impact on third and developing countries (IA, p. 63-64 and Annex 4, p. 95-100). It was subsequently ‘complemented’ in response to RSB comments (follow-up document, p. 20-23), but this assessment would have benefited from more attention given the strong external dimension of the proposal. Indeed the IA underlines that ‘the most salient adverse impacts on human rights and on the environment occur mainly outside the EU’ (IA, p. 63).

Third countries that are expected to be the most impacted by this initiative include the main EU trading partners and those where sustainability standards are generally lower.

Based on various studies, the IA expects some positive impact, such as on improved labour and human rights, environmental practices, increased stakeholder awareness and adoption of international standards, better access to remedy for victims of abuse and economic benefit for local communities (IA, Annex 4, pp. 95-100).

In terms of negative impact, the follow-up document raises the risk of disengagement (termination of the business relationship) but envisages safeguards to mitigate this (see follow-up, p. 23).

The revised scope directly covers some non-EU companies (4,000 companies, according to the Commission’s estimate), which are expected to incur €240 million recurrent and €70 million initial procedural compliance costs (follow-up, p. 18, pp. 20-23). Third-country companies and economies outside the scope are also expected to be indirectly affected through global value chains.

Impacts on national budgets and administrations

Under the revised scope, the annual supervisory costs for (existing or newly set up) public authorities to be designated by Member States to monitor and enforce compliance, are expected to be lower than in the IA’s preferred options. The Commission estimates total recurrent supervisory costs in the EU to reach around €5.55 million a year, with initial costs of €130,000 (follow-up, p. 18).
Monitoring and evaluation

The IA (p. 89-90) and the proposal (COM(2022) 71, Article 10 p. 58) are vague on the set of qualitative and quantitative indicators that will be used to monitor progress towards the general and specific objectives. In particular, the IA acknowledges that 'monitoring progress towards meeting the general objectives as such is very complex, since it would be methodologically challenging to distinguish between the impacts of the proposed initiative and other possible causes'.

The IA plans that the Commission will carry out an evaluation of the IA’s preferred options and issue an evaluation report five years after the end of the transposition period, 'taking into account the time needed for application and data collection'. In the proposal (p. 23), the Commission plans to report on the implementation of the directive after seven years, including on its effectiveness.

Stakeholder consultation

The Commission refers to stakeholders' views fairly consistently in the IA. The consultation strategy (IA, Annex 2, pp. 12-30) was built on several components:

- The inception IA (roadmap) from July 2020 to October 2020, receiving 114 items of feedback;
- Social partners (employers’ organisations, trade unions) consultation in February 2021;
- A number of stakeholder workshops and meetings (e.g. with company law experts; business associations; individual businesses, including SMEs representatives; and civil society, including non-governmental and not-for-profit organisations as well as the OECD).
- A 15-week open public consultation (OPC), from 26 October 2020 to 8 February 2021.

The OPC results are described in Annex 2 of the IA. A more extensive summary report and detailed contributions are also publicly available. There were 473 461 public responses to the OPC, and 149 position papers received. The IA also highlights that the vast majority of responses (472 606) was submitted through non-governmental organisation (NGO) campaigns, using a methodology known as ‘key-collision clustering algorithm’ and pre-filled questionnaires, that were analysed separately, as recommended in the BRG (Tool #54).

The remaining 855 responses came from NGOs, companies, business associations, and EU citizens. Only 6.6% of the respondents were from non-EU countries other than the United Kingdom and United States, and only a few were received from developing countries. Stakeholders’ views are broken down into groups only in case of differences in the opinions (IA, p. 68). Opinions from SMEs are presented in Annex 5 (IA, part 2, pp. 109-111). Concerning corporate due diligence, 92% of stakeholders across all groups supported the need for a horizontal EU legal framework. Regarding the scope, 97% of respondents agreed that the DD rules should also apply to third-country companies. For its enforcement, 71% indicated supervision by a national authority as the best-suited option. Regarding directors’ duties, the majority of respondents across all groups recognised the need to take account of stakeholders’ interests in corporate decisions, and especially to integrate them into a company’s strategy (86% of respondents). Opinions diverged more on setting measurable targets and balancing stakeholders’ interests, on which individual companies and business associations mostly expressed concern and disagreement. Some half the respondents gave their opinion on directors’ remuneration and the IA indicated that ‘a large group of respondents expressed disagreement’ (not further specified) on this part of the initiative (Annex 2, p. 20). Petition and campaign responses are overall consistent with NGO positions analysed in the OPC. Petition signatories and most position papers agreed that the directive should apply to all businesses, regardless of their size. On this point, the IA notes that while civil society organisations in the OPC overwhelmingly supported the need for the establishment of cross-sectoral mandatory due diligence obligations for all companies, independent of their form or size and whether domiciled or operating within the EU (part 2, p. 14), ‘different types of companies and business associations have called for a cautious, gradual and proportionate approach in order to take into account the impact on SMEs’ (part 2, p. 109). The follow-up document would have benefited from showing the extent to which the revised options are supported by stakeholders across groups.
Supporting data and analytical methods used

The IA refers to various sources of information used in its preparation (IA, part 2, pp. 7-11):

- **External expertise** to provide advice and analysis for the IA and OPC results;
- A bibliography of economic and research reports;
- Data and reports from EU and international organisations (Eurostat, OECD, ILO, etc.);
- Two supporting studies on due diligence requirements through the supply chain and directors’ duties and sustainable corporate governance, prepared in 2020.

To consider the specific situation of SMEs, a more recent study on the uptake of corporate social responsibility (CSR) by European SMEs and start-ups, from December 2021, was used in the IA (its preliminary findings) and in the follow-up (final report). According to this study, most SMEs (97%) perform some kind of activity that can be labelled, to various extents, as CSR. The study also shows the key drivers and barriers to CSR and sustainability uptake.

Overall, this IA is based on a good review of literature, and data sources are referenced clearly. The IA explains methods for the analysis. Estimates of the number of companies under the scope of the directive are based on firm-level data derived from the Orbis database. Estimation of costs is mainly based on stakeholder consultation conducted in the supporting study on DD, and results were cross-checked with other IAs. The IA acknowledges some limitations to quantifying costs of DD measures, mainly due to difficulties for businesses to estimate costs, to distinguish newly generated costs from ‘business as usual’, and because some activities are too closely interlinked. The IA adds that benefits, including the expected positive human rights and environmental impact, ‘cannot be expressed in monetary terms’. (Annex 3, p. 32). The follow-up document adds that experience is also limited, because DD is so far mostly implemented on a voluntary basis and in the few countries that have legislated, it is too early to assess change on the ground.

While the Commission is transparent about the revision of the scope of the IA’s preferred options following the negative RSB opinions, alternative definitions of company groups (for example to justify the choice of turnover threshold) could perhaps have been compared, as this strongly affects the number of companies under the scope of the directive, as well as its coherence in terms of scope and content with other existing rules, such as CSRD. The Commission estimated that ‘the changed approach to define high-impact sectors and the increase of applicable minimum size thresholds result in a decrease of the total number of EU companies in the scope to about 12 000’. (follow-up, p. 42). This represents a significant decrease compared to the IA’s preferred options, as the Commission had estimated 70 000 companies under option 3a and almost 59 000 under option 3b. Based on thresholds defined (only in the proposal) for third-country companies active in the EU, the scope covers an additional 4 000 non-EU companies (follow-up, p. 13).

**Follow-up to the opinion of the Commission Regulatory Scrutiny Board**

The IA was submitted to the RSB on 9 April 2021 and received a negative opinion on 7 May 2021. The RSB’s general comments concerned: 1) the vague problem description, failure to demonstrate the magnitude and likely evolution of the problem and lack of clear evidence that EU business (including SMEs) do not sufficiently address sustainability opportunities, risks and impacts; 2) over limited policy options and failure to adequately reflect the policy choices available in terms of company and sector scope, content of measures and range of delivery instruments; unclear added value and effectiveness of several measures; 3) insufficient assessment of proportionality and presentation of costs and benefits; 4) insufficient integration of differentiated stakeholder views.

While noting a ‘significant revision’, the Board maintained a negative opinion on the revised IA on 26 November 2021, as the report still contained some ‘significant shortcomings’ (SEC(2022) 95, p. 1, p. 5). The RSB maintained the three first criticisms, adding that ‘impacts are not assessed in a sufficiently complete, balanced and neutral way. Uncertainty related to the realisation of benefits is not sufficiently reflected’. In addition, the RSB made 19 specific comments.
The IA was not revised a second time, but complemented with a separate staff working document, as a follow-up to the RSB second opinion. While this choice is explained for transparency reasons, it makes the IA and its link with the proposal more difficult to follow, especially due to the revision of the IA’s preferred options. The Commission made an effort to take comments from the RSB into account, explaining in tables how and where each one was addressed following the first negative opinion (IA, Annex 1, pp. 1-11) and the second (follow-up, pp. 41-53).

According to the latest version of the BRG (p. 31), ‘where the RSB issues two negative opinions, only the vice-president responsible for “better regulation” can give the green light for the adoption of the initiative’ (emphasis added). It was decided to proceed with this initiative due to its political importance, the urgency for action, and to address the risk of increasing fragmentation of the single market.

**Coherence between the Commission’s legislative proposal and IA**

Due to the changes made by the Commission following the two negative opinions from the RSB, the following main elements of the proposal differ from the IA (follow-up document, pp. 6-17, pp. 42-52 and COM(2022) 71, explanatory memorandum, pp. 19-23):

- The directive’s objectives were revised in the proposal, in particular the part related to directors’ duties was removed from the objectives (see section on ‘Objectives’);
- On corporate due diligence, the personal scope of the IA’s preferred option was considerably reduced (exclusion of SMEs and smaller midcaps, reduced number of high-impact sectors);  
  - Directors’ duties were also significantly reduced, focusing on directors’ duties relating to putting in place and overseeing due diligence. Other specific duties that were part of the IA’s preferred option, were not retained;
- Rules on directors’ remuneration were not retained, apart from the obligation to take account of the emission reduction plan when setting directors’ variable remuneration.

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The impact assessment (IA) accompanying the proposal on corporate sustainability due diligence received two negative opinions from the Commission’s Regulatory Scrutiny Board. Additional evidence was provided in a follow-up document to the Board’s second opinion, explaining how the IA’s preferred options were revised in the proposal, but no change was made to the IA itself. The IA cannot therefore be read without this follow-up document. It also makes the analysis quite difficult to follow, as evidence is split between several documents that are not consistent.

Overall, this IA is well substantiated with economic literature and analysis reports, including two supporting studies from 2020. The IA is transparent on the methods, assumptions and limitations of the analysis. The IA refers to stakeholders’ views fairly consistently, but it seems that only a limited number of stakeholders from third and especially developing countries were consulted. The problem identified in the IA covers two dimensions of sustainable corporate governance, and the objectives defined are directly linked to the problem. In the IA, policy options are identified across three areas: corporate due diligence, directors’ duties and their remuneration. The IA focuses on the assessment of the economic impact. Costs are estimated for companies and public authorities, while expected benefits are described in a qualitative way. Other types of impacts (social, environmental, and on human rights) that are particularly relevant in this initiative, are analysed less extensively.

The Commission made efforts to take account of comments from the RSB, but some weaknesses remain. To respond to proportionality concerns from the Board, the IA’s preferred options were revised. However, different alternatives could have been compared for the revision of the IA’s preferred options. As revised in the proposal, the options focus on the due diligence duty, leaving out part of the directors’ duties and of the rules on directors’ remuneration. The objectives were also revised, focusing on one (the external) dimension of the problem. As the number of companies under the scope of application was reduced under the revised options from up to 70 000 estimated in the IA to around 12 000 EU companies (in addition to 4 000 non-EU companies), the costs for companies were significantly reduced and recalculated in the follow-up document. The analysis of
impacts on third and developing countries was also 'complemented' in the follow-up to RSB comments, but this assessment would have benefited from more attention, given the strong external dimension of the proposal. For future monitoring and evaluation of the initiative, the indicators envisaged, as well as the related timelines and target would benefit from clarification.

ENDNOTES


3 In the 2021 Commission work programme and in the Inception Impact Assessment.

4 Minerals in the Conflict Minerals Regulation and in the proposal for a new Batteries Regulation, timber under the EU Timber Regulation, and some additional agricultural commodities in the proposal on deforestation-free products.

5 In the Swedish Riksdag opinion, the provisions that companies shall duly take into account including: the fulfilment of obligations when setting variable remuneration (Article 15.3), provisions on company directors' duty of care (Article 25), and the introduction and oversight of due diligence (Article 26); are incompatible with the principle of subsidiarity.

6 For group 1, the proposal specifies that account should be taken of the company's plan to ensure that its business model and strategy are compatible with the transition to a sustainable economy and to the EU's climate commitments in directors' variable remuneration.

7 For group 1, the criteria defined in the IA (p. 46) are: i) option 2a: 500+ employees OR €350 million+ turnover, ii) option 2b: 50 to 500 employees AND €150 million+ turnover. In the Commission proposal: (article 2), group 1 is similar to option 2b.

8 In the IA, the threshold for turnover generated in the EU is not set. In the proposal, it is aligned with groups 1 and 2.

9 For group 2, the criteria in the IA (p. 46 and Annexes) are: i) option 2a: 50 to 500 employees AND €8 million to €350 million turnover in high impact sectors, ii) option 2b: 50+ employees AND €8 million+ turnover in high impact sectors, but smaller than group 1, option 3b. In the proposal, (article 2), group 2 is defined as 250+ employees AND €40 million+ turnover (with at least 50 % in high impact sectors).

10 The IA was prepared on the basis of the BRG in force at the time (2017 version). The summary of benefits and costs of the preferred option was revised according to the most recent version of the guidelines (November 2021 update), with a separate table for the implementation of the ‘one in – one out principle (SWD(2022)39, p. 17).

11 Multiple respondents ‘found the online questionnaire to be biased and difficult to answer’ and expressed their view in a position paper (IA, Annex 2, p. 25).

12 Several stakeholders expressed concern regarding the methodology used in this supporting study. The need for legislative intervention on directors' duties as such was called into question, ‘as it might put into question the fundamentals of freedom of enterprise and property/ownership’ (IA, p. 82).


This briefing, prepared for the EP Committee on Legal Affairs (JURI), analyses whether the principal criteria laid down in the Commission's own Better Regulation Guidelines, as well as additional factors identified by the Parliament in its Impact Assessment Handbook, appear to be met by the IA. It does not attempt to deal with the substance of the proposal.

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