

Ceemet's views on the Commission's proposal for a Directive on Corporate Sustainability Due Diligence

On 23 February 2022, the Commission published its proposal for a Directive on corporate sustainability due diligence. Ceemet is strongly concerned about the negative effects that this Directive will have on European companies in terms of competitiveness as our companies will be in an enormous competitive disadvantage in comparison to third country companies that are not subject to these heavy administrative burdens proposed by the Commission.

Key messages

- Ceemet acknowledges that companies have a responsibility to take social, environmental and human right issues into account in addition to their financial performance and adhere to existing legal frameworks, with many already taking voluntary action. Yet this should be reached by a proposal which is workable in practice and does not cause an overwhelming amount of administrative and financial burden on companies. Especially the MET sector has very complex products with very long global supply chains and would be heavily affected by the proposal. We call on the European institutions to find an approach which does maintain the aim of the Directive, while making it workable for EU companies.
- The proposal will cause a significant amount of administrative burden on companies. It is therefore of key importance that the Directive will only apply to large companies, i.e. companies which have over 1,000 employees and the obligation to carry out due diligence must be limited to the first tier of the companies' supply chain located outside of the EU.
- The Directive compromises the need for legal certainty as it includes vague concepts and insufficiently concrete definitions such as the definition on 'established business relationship' and 'value chain', which leave too much room for interpretation. The need for legal certainty is fundamentally put at risk by the article on civil liability.
- The proposal entails a major risk of fragmentation of legislation within the EU as there is too much leeway for Member States to differently interpret the text of the Directive. Companies which act on the European Single Market need common rules to preserve the competitiveness of European business. Ceemet strongly advocates for the text of the Directive to be clarified so that there are no discrepancies between the transposition laws of the Member States.
- As a more principled objection, Ceemet underlines that it is unreasonable that companies have to take over the traditional role of the governments in ensuring adherence to rules and introducing liability for other third parties' action. Companies do not have the mandate nor the capability to solve all the problems arising from weak governance.

- It is important that public companies set the example as regards due diligence obligations and they should therefore explicitly fall in the scope of the Directive.

General remarks

Ceemet acknowledges that companies have a responsibility to take social, environmental and human right issues into account in addition to their economic and financial performance. European companies take the stakeholders' interests into account when taking decisions, notably those affecting the financial interests of shareholders as they expressly recognise their responsibility on these important issues.

European companies are world leading in monitoring supply chains' adherence to human rights and environmental protection. For instance, many Ceemet members already include environmental, social, and corporate governance ("ESG") factors in their ongoing due diligence measures through robust and tested frameworks, such as the UN Guiding Principles on Business and Human Rights and the OECD guidelines, and mandatory regimes, such as the UK and Australian Modern Slavery Acts, the obligations in relation to Conflict Minerals and the EU Non-Financial Reporting Directive.

The Due Diligence Directive cannot be seen separately from these tools and coherence with already existing legislation is crucial. Unfortunately, the Directive as proposed by the European Commission will create a significant amount of additional obligations on companies and will cause a lot of legal uncertainty. Consequently, the proposal will inevitably have a critical impact on European based companies, their operations and supply chains, as well as on their global competitiveness. We see this proposal as a clear breach of the "one in, one out"-principle to which the Commission committed itself.

Finally, Ceemet underlines that it is unacceptable for the Commission to propose that companies have to take over the traditional role of the governments in ensuring adherence to rules and introducing liability for other third parties' action. Companies do not have the mandate nor the capability to solve all the problems arising from weak governance that may, for instance, cause human rights breaches in foreign supply chains.

Far reaching legislation could have unwanted consequences, such as dampening investment in third countries as European companies will feel forced to withdraw from these countries due to legal uncertainty and liability risks. This risks less growth and more poverty in such countries and potentially even lower environmental and human rights standards there.

Specific remarks as regard content of the Directive

1) High increase of administrative burden – Need for a workable solution for companies

The proposal will cause an overwhelming amount of administrative burden on companies. It is therefore of main importance to find an approach which is workable in practice for companies.

a. Scope

The Directive, as proposed by the Commission, entails very extensive obligations on companies such as the obligation to carry out due diligence across the entire value chain and carry out assessments at least once every 12 months.

This will inevitably impose heavy additional administrative costs and procedural burden on companies. Even for big companies it will be a challenge to fulfil the additional obligations in this regard. Smaller companies, which often have fewer resources, should be excluded or will otherwise have to shift a lot of their time and resources from their core corporate activities to carrying out due diligence.

Therefore, Ceemet is of the opinion that only companies that **employ more than 1,000 employees** should be considered to fall under the scope of the Directive, rather than companies that employ over 500 employees (art. 2 §1 a). This practice would be fully in line with existing EU legislation such as the German Supply Chain Act. The French Loi de vigilance even has a threshold of over 5,000 employees.

Furthermore, although we appreciate that Small and Medium Enterprises are in principle out of the scope of the Directive, we note that the **SMEs will in any case be highly impacted** by the Directive as they are often in the supply chain of larger companies and will therefore be highly affected due to the trickle-down effect. This will create a disproportionate amount of administrative burden on them which will moreover be very cost-intensive. Ceemet therefore proposes to limit the obligation to carry out due diligence to the first tier of the companies' supply chain located outside of the EU. This would ensure that SMEs within the EU are really exempted from the scope – and are not indirectly affected by the legislation through their business partners as it is the case with the Non-Financial Reporting Directive.

While the proposal includes support for SMEs caught by the requirements, it is essential that the Commission and public authorities have a role in assessing the impact in different sectors and different countries. It should not be left to companies to assess the impact and to apply European standards to operators in third countries. Ceemet calls on the Commission to publish on a 12 month basis a full assessment of risks in key sectors in third countries to help companies in assessing their own risks.

Ceemet notes that the **list of high impact sectors** (art. 2 §1 b), as proposed by the Commission, aligns to some extent with the NACE Code the standard European nomenclature of productive economic activities. However, it also includes a reference to a wider definition including the “wholesale trade” in goods from these sectors. It is essential for companies to understand explicitly whether they are in scope or not. For reasons of legal certainty, Ceemet proposes to explicitly reference the list of the applicable code of the sector in the text of the Directive, limiting the list to specific parts of sectors which represent a risk. As part of the Commission's annual risk assessment should list relevant sectors and third countries which represent high-impact sectors.

Moreover, a clear distinction should be made between the extraction of metals and their primary transformation and other metallurgical activities. It is excessive to cover the second transformation of metal products (i.e. the manufacture of basic metal products, other non-metallic mineral products and fabricated metal products). This would amount to carrying out due diligence on products that do not present significant risks for human rights or the environment, such as hairpins and other products containing residual metal. It would then be appropriate to exclude the secondary transformation of metals, which includes all manufactured products containing metal for the economy and not only "machinery and equipment".

Finally, an **unjustifiable distinction is being made between private companies and the public sector** as they fall outside the scope of the proposed Directive. We do not see any valid reason for this distinction as both entities are equally concerned by the challenges related

to due diligence. Private companies are entitled to expect that the State and its contracting entities will set the example as regards due diligence obligations.

b. Due diligence on the entire value chain

The requirements to carry out due diligence for the entire value chain, both upstream as well as downstream, as proposed by the Directive is quite simply unworkable, also for larger companies as it is impossible to manage all the risks related to all of their direct and indirect suppliers. Large companies sometimes have over 100.000 direct suppliers and further upstream suppliers could comprise millions of micro-companies. Moreover, it is completely unreasonable to require companies to control their value chain as it is not in the hands of companies to control and take legal responsibility for their customers' action.

This will put European based companies in an enormous competitive disadvantage in comparison to third country companies which are not subject to these heavy administrative burdens.

Ceemet therefore considers that the Directive must ensure that the obligation to carry out due diligence is **limited only to the first tier of the companies' supply chain**, i.e. with which companies have a direct contractual supplier relationship. This approach is in line with other national legislation on due diligence, such as the French and German frameworks and would therefore not disrupt the functioning of national systems.

Furthermore, it is of crucial importance that the obligation to carry out due diligence is **limited to the tier-1 suppliers located outside of the EU** as a targeted scheme is risk-based and therefore more efficient and effective. There are already very high standards in the EU as regards environment and human rights and also effective systems of control and enforcement in place in the EU Member States. Therefore it has little to no added value for companies within the EU to carry out due diligence on each other but it will create an enormous amount of administrative burden on them. We underline that this approach was already taken in the Conflict Minerals Regulation and proved to be effective.

2) Provide for legal certainty

a. Vague definitions and concepts

The Directive includes vague concepts and insufficiently concrete definitions, which leave too much room for interpretation and will inevitably cause legal uncertainty on companies:

- **'established business relationship'** (art. 3f): The notion of the established business relationship is extremely unclear, especially as it refers to an 'indirect' business relationship. This definition raises several questions and gives too much leeway to Member States to fill in these questions according to their own interpretation and could therefore strongly differ from other Member States' interpretation. Ceemet considers that the definition should be limited to tier-1 suppliers in an explicit and direct contractual relationship only and not throughout the entire value chain.
- **'value chain'** (art. 3g): The proposed definition of value chain is very extensive as it does not only include the original supplier, but also all other companies in the chain, both upstream as well as downstream. Ceemet therefore suggests to replace the notion of "value chain" by "supply chain" throughout the Directive.
- **'stakeholder'** (art. 3n): The definition of stakeholder is too broad and basically entails anyone, whether they truly have legitimate interest or not. Read in conjunction with other articles (e.g. art. 6§4, art. 7§2a and art. 8 §3b) this would imply that companies will

need to carry out consultations to gather information on adverse treatment and in the developments of their action plans with possibly anyone. In combination with the extensive provisions on civil liability, this will open the door for abusive and excessive litigation if this power is given to such a wide range of people. Ceemet therefore strongly suggests to redefine this notion and narrow it down to people that have a true legitimate interest in this matter.

b. Civil liability

Article 22 on civil liability, as proposed by the European Commission, fundamentally compromises the need for legal certainty as it risks to open the door for abusive and excessive litigation.

It should be noted that companies can only be liable for damages which they directly cause or at least that they can directly control or influence. They cannot directly control the actions of their contractual business partners and even less so the actions of tier x suppliers along the supply chain. The civil liability of one company should end where the actions of a legally independent third party begin. At most, Ceemet believes that it could be acceptable to establish civil liability for companies as regards their direct suppliers.

Furthermore, the traditional civil liability rules should apply in this respect and companies can therefore only be liable if (i) they have not carried out due diligence measures at all, (ii) there is damage and (iii) there is a causal link between these two conditions. In case it is not a requirement for these conditions to be fulfilled, it will cause an extreme amount of legal uncertainty on companies. This while legal certainty, especially with respect to civil liability, is a prerequisite for a successfully doing business.

Finally, as stated above with regard to the definition on stakeholder, the notion is also extremely problematic in the context of civil liability. As this broad definition of stakeholder read in conjunction with the article on civil liability will open the door for abusive and excessive litigation.

3) Fragmentation of legislation – Need for a level playing field

The tech and industry employers agree that there are advantages to a harmonised EU framework on due diligence. We are of the opinion that it is of crucial importance that the level playing field is preserved and thus, the possibility for Member States to deviate from the EU legislation during the implementation process must be avoided at all costs.

As mentioned under point 2 of this paper, this Directive lacks clarity caused by vague concepts and insufficiently concrete definitions. Therefore, Ceemet fears that there will be too much leeway for Member States to differently interpret the text of the Directive which could result in discrepancies between national transposition laws. This does **not guarantee a level playing field within the EU** and even undermines the aim of the proposed legal basis (i.e. Article 50 TFEU), which is to fight legal fragmentation to ensure one of the right of establishment, fair competition and ultimately to stimulate sustainable investment.

We cannot end up with companies having to comply with 27 different national due diligence legislations, particularly key for multinational companies operating in multiple jurisdictions. Instead, we need common rules to preserve the competitiveness of European business and avoid the distortion of competition rules.

Especially our big member companies (e.g. in the automotive sector) have production sites in many different EU Member States. Many of these subsidies would qualify under the Directive

by themselves – therefore, the subsidies would fall under the respective national due diligence law. It makes no sense that different national due diligence laws will apply to the identical product only on the basis of where within the EU the product was finally assembled. Ceemet strongly advocates for the text of the Directive to be clarified so that there are no inconsistencies between the transposition laws of the Member States.

Moreover, there is also a need for a **better level playing field between EU companies and third-country companies**. Where EU companies fall under the scope of the Directive when they have a turnover of over 150 million € worldwide (Art. 2§1 a), the legislation only applies to third-country companies if they have a turnover of over 150 million € within the EU (Art. 2§2). Consequently, the legislation will apply to many more smaller EU companies than third-country companies. This will put EU companies in a strong competitive disadvantage in comparison to said third-country companies. Ceemet therefore proposes that the turnover for both European as well as third-country companies is calculated on what is generated within the European Union.
