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NOTE

From:	General Secretariat of the Council
To:	Permanent Representatives Committee
No. Cion doc.:	6533/22
Subject:	Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on Corporate Sustainability Due Diligence and amending Directive (EU) 2019/1937 - Guidance for further work

I. INTRODUCTION

1. On 23 February 2022, the Commission submitted to the European Parliament and to the Council a proposal for a Directive on Corporate Sustainability Due Diligence and amending Directive (EU) 2019/1937¹.
2. The proposed Directive, based on Article 50 and Article 114 of the TFEU, lays down rules on obligations for companies regarding actual and potential human rights adverse impacts and environmental adverse impacts, with respect to their own operations, the operations of their subsidiaries, and the value chain operations carried out by entities with whom the company has an established business relationship. It also lays down rules on liability for violations of these obligations.

¹ 6533/22 + ADD 1

3. The proposed Directive aims to set out a horizontal framework to foster the contribution of businesses operating in the single market towards the achievement of the Union's transition to a climate-neutral and green economy in line with the European Green Deal and the UN Sustainable Development Goals.
4. The European Parliament's Committee on Legal Affairs (JURI) appointed Ms Lara WOLTERS (S&D, NL) as rapporteur on the proposal, with eight committees being asked for an opinion namely, the Committee on Development (DEVE), the Committee on the Internal Market and Consumer Protection (IMCO), the Committee on Industry, Research and Energy (ITRE), the Committee on Foreign Affairs (AFET), the Committee on the Environment, Public Health and Food Safety (ENVI), the Committee on Economic and Monetary Affairs (ECON), the Committee on International Trade (INTA), and the Committee on Employment and Social Affairs (EMPL), the latter five being associated committees. The JURI Committee is expected to vote on its amendments to the Commission proposal and adopt the mandate for negotiations at the end of March 2023, with the negotiating mandate expected to be voted at plenary in May 2023.
5. The opinion of the European Economic and Social Committee was adopted on 14 July 2022².

II. WORK WITHIN THE COUNCIL

6. The Council at its meeting of 24 February 2022, heard a presentation from the Commission on the content and aim of the proposed Directive.
7. The Company Law Working Party started examining the proposal under the French Presidency in March 2022 with a presentation of the proposal by the Commission. A detailed examination of the Commission's proposal ensued at five Working Party meetings. The work continued during the Czech Presidency starting with the Working Party meeting of 12-13 July 2022, with the first compromise text being examined at the Working Party meeting of 5-6 September 2022. Discussions have pursued in two subsequent Working Party meetings on 26-27 September and 18-19 October 2022.

² 11489/22.

8. The impact assessment accompanying this proposal was examined on 3 and 21 March 2022, on the basis of the indicative checklist developed to examine Commission impact assessments in the Council. Discussions focused on issues on which delegations requested further clarifications. Following the explanations provided by the Commission, the Working Party proceeded with the examination of the proposal.
9. Following the discussions at Working Party level, the Presidency has amended several provisions of the Commission's proposal to take account of delegations' requests. On this basis, the latest compromise text prepared by the Presidency is set out in document 13256/22. All delegations have a general scrutiny reservation on the text.

While delegations support overall the objectives of the proposal, their views still differ on how best to achieve those objectives. The Presidency endeavoured to improve the proposal's clarity, feasibility and provide legal certainty. However, the Presidency deems necessary to further assess the situation on some of the key issues of the proposal and requests the Permanent Representatives Committee for political guidance on the most suitable way forward on the three below-mentioned issues.

III. ISSUES FOR POLITICAL GUIDANCE

10. The Presidency sets the following three issues for discussion and outlines the possible options to reach a compromise on each of them. The Permanent Representatives Committee is invited to express their preference for Option A or B as a way forward on each issue.

Scope: 'individual approach' or 'consolidated approach' (Article 2)

11. Article 2 establishes the personal scope of application of the proposed Directive and sets out the criteria based on which the companies that would fall under the due diligence obligations are determined (Article 2(1) and (2)). The criteria are based on the number of employees and the net worldwide turnover for EU companies, and on the net turnover generated in the Union for non-EU companies: In the latest compromise text prepared by the Presidency, as set out in document 13256/22, the criteria for non-EU companies were changed to a net worldwide turnover provided that a significant part was generated in the Union.
12. The Working Party has extensively debated the issue of whether fulfilment of the thresholds set under those criteria should be assessed on a consolidated basis, so that the number of employees and the net turnover of subsidiaries are taken into account, or on an individual basis at a company level, so that the number of employees and net turnover are assessed for every company as a single entity: Delegations are divided in their views as to which approach would be the most appropriate. The Presidency has proposed two options, as below. The actual levels of thresholds of the number of employees and the net turnover are still to be discussed at Working Party level.

Option A:

13. Individual approach: some delegations pointed out that this approach could raise the possibility of companies circumventing the obligations set out in the proposal by setting up subsidiaries for the sole purpose of transferring to them a number of employees and/or business relationships to reduce their own number of employees and/or net turnover at individual level in order not to fall under the scope of the proposed Directive.

Option B:

14. Consolidated approach: this approach complicates the identification of companies falling under the scope of the proposed Directive by the supervisory authorities of the Member States. The consolidated approach would also entail that the scope of application would be extended because more companies would fall under the scope of the proposed Directive, if the thresholds stayed the same. However, the number of such companies is not possible to determine or credibly estimate as there are no relevant data available from the existing databases. Nonetheless, in the latest compromise text prepared by the Presidency set out in document 13256/22, the thresholds were proposed to be raised, should the consolidated approach be supported.

Definitions: ‘established business relationship’ or ‘business relationship’ (Article 3(f))

15. The proposed Directive lays down rules on due diligence obligations for companies with respect to their own operations, the operations of their subsidiaries, and the value chain operations carried out by entities with whom the company has an established business relationship, as set out in Article 1. The concept of ‘established business relationship’ is a key element of the proposal limiting the scope of business relationships in their value chains in respect of which the due diligence obligations are carried out. Several delegations have expressed concerns about this concept and have called for greater alignment with international standards which do not recognise this concept. The Presidency has proposed two options:

Option A:

16. Delete the concept of ‘established business relationship’ which would emphasize the need for a risk-based approach and align more with the international standards, namely with the United Nations Guiding Principles on Business and Human Rights (UNGPs), and the OECD Guidelines for Multinational Enterprises, which are accompanied by the OECD Due Diligence Guidance for Responsible Business Conduct (OECD Guidance). Deletion of the concept would entail that companies would have to carry out due diligence obligations in respect to all business relationships in their value chains, which is why the risk-based approach and the prioritisation as strengthened in the latest Presidency compromise text set out in document 13256/22 become of key importance and effectively limit the breadth of due diligence obligations of companies at one point in time.

Option B:

17. Keeping and clarifying the concept of ‘established business relationship’ as amended in the latest Presidency compromise text set out in document 13256/22. As pointed out by some delegations, keeping the concept in the proposed Directive might incentivise companies to change their contract policies, for instance, by entering into short-term contracts or changing their suppliers more frequently. Also, it might complicate the determination of business relationship in their value chains in respect of which the company should carry out due diligence obligations, not only by companies but also by supervisory authorities of Member States, due to the necessity to first analyse whether or not the business relationship is ‘established’.

Definitions: ‘value chain’ or ‘supply chain’ (Article 3(g))

18. The proposed Directive defines ‘value chain’ as covering activities related to the production of goods or the provision of services by a company, including the development of the product or the service and the use and disposal of the product as well as the related activities, upstream and downstream of the established business relationships of the company. The definition also takes into account specificities of providing financial services by regulated financial undertakings. A number of delegations have asked for substantial changes to the definition of value chain, including changing the concept to ‘supply chain’ so as to limit it to the upstream part only. The Presidency has proposed two options:

Option A:

19. Keeping the concept of ‘value chain’ but with some amendments to its definition to limit the downstream part in order to ensure feasibility, for example by excluding consumers from the value chain or limiting the use of the product only to the intended or reasonably foreseeable use. The latest Presidency compromise text in this regard is set out in document 13256/22. Nonetheless, some delegations argued that companies do not have a sufficient leverage as regards their downstream business relationships and cannot control and enforce the fulfilment of due diligence obligations by them.

Option B:

20. Changing the concept of 'value chain' to 'supply chain' which would reduce the material scope of the proposed Directive, even though the adverse impacts occur also in the downstream part of the value chains. Moreover, limiting the scope of the proposed Directive to supply chains could lead to a significant reduction of the aims in respect to financial undertakings that provide financial services as part of the downstream activities.

IV. CONCLUSION

21. The Permanent Representatives Committee is invited to provide guidance on the above-mentioned issues.
 22. The guidance will allow the Presidency to continue work towards reaching a General Approach at the Council meeting (Competitiveness) on 1 December 2022.
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