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The Highly Debated Corporate Sustainability Due Diligence Directive at Risk of a Definitive Block

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Introduction

On February 28, 2024, the Council of the European Union (EU) failed to attain the anticipated qualified majority for endorsing the provisional agreement reached on December 14, 2023, with the European Parliament concerning the Corporate Sustainability Due Diligence Directive (CSDDD) legislative proposal. The absence of endorsement from the Council of the EU (Council) hinders subsequent endorsement by the relevant committee of the European Parliament – a necessary step before formal adoption of the law by the European Parliament and the Council. As the mandate of the European Parliament is coming to an end, this procedural deadlock might result in the non-adoption of the CSDDD during this legislative term, creating uncertainty regarding the fate of the directive itself.

Background

The CSDDD aims to shift corporate responsibility from a voluntary to a mandatory framework, intending to integrate environment, social and governance (ESG) due diligence obligations for EU companies within its scope and, under certain conditions, outside the EU. Specifically, under the proposed rules, companies would be required to identify potential and actual adverse impacts on ESG related to their operations, subsidiaries and business partners within their value chain.

Due to its significant implications for large corporations, the CSDDD has garnered attention from stakeholders, including industries and nongovernmental organizations (NGOs). This attention has influenced the legislative process, leading to numerous discussions and attempts to reach agreements during the adoption phase within the European Parliament and the Council.

Conclusion of a Provisional Agreement

In spite of the challenging journey, the two co-legislators (i.e., the European Parliament and the Council) reached a provisional agreement on December 14, 2023. The provisional agreement indicated that the co-legislators had found common ground on contentious aspects of the law, including the inclusion of companies within the legislation's scope, applying obligations to the financial sector, and outlining penalties and civil liability for noncompliance.

As outlined in the press release from the Council (the text of the provisional agreement is not yet public), key points agreed upon so far by the co-legislators include:

- **Scope of the Directive** – The provisional agreement covers both EU-based companies and those from third countries, subject to specific thresholds of employees and turnover. Lower thresholds would apply for companies in certain "high-risk sectors," such as textiles, clothing, agriculture, food manufacturing and raw materials trade.
- **Financial sector** – Financial services are temporarily excluded from the directive's scope, with a review clause for potential inclusion based on a future impact assessment.
- **Civil liability** – The agreement establishes a five-year period for bringing claims by those affected by adverse impacts, with limitations on evidence disclosure, injunctive measures and claimant-proceeding costs. A contentious element that has also been agreed through the negotiations is to remove director's duty of care altogether from the final text.
- **Penalties** – The provisional agreement includes injunction measures and considers the company's turnover to impose pecuniary penalties, with a range of up to 5% of the company's net turnover.

Blockage in the Adoption of the Law

After the provisional political agreement reached last year, technical negotiations to iron out certain provisions of the law particularly regarding recitals continued and concluded at the end of January 2024. According to an established practice, after interinstitutional negotiations (also known as trilogues) are concluded by the two co-legislators and the European Commission, the law's text remains unchanged. However, as already observed in other cases during the current legislature (e.g., the "End of Combustion Engine" law – Regulation (EU) 2023/851), there has been a trend for the Council to reassess or oppose the text even after reaching a provisional agreement, after certain Member States express post-negotiation reservations to the agreed text.

In terms of procedure, following the provisional agreement between the two co-legislators, an informal adoption by the Council is necessary. In this case, the adoption is carried out by the Permanent Representatives Committee (COREPER I). Subsequently, the European Parliament endorses the agreement in the committee leading the file, which, in this case, is the Committee on Legal Affairs (JURI). The text shall then be submitted for the judicial linguist review and translation to the remaining 23 EU languages. The post-judicial linguist text needs to be endorsed by the European Parliament plenary followed by the Council in any ministerial configuration.

At the current stage, the CSDDD was awaiting the informal endorsement by the 27 EU ambassadors so that the file could be sent to the relevant committee of the European Parliament JURI committee for its endorsement and continuation of the next procedural steps. However, the "qualified majority" (i.e.,15 EU countries representing 65% of the EU population) required for the endorsement in the Council has not been reached. The primary opponent to the adoption of the law has been Germany, influenced by the Free Democratic Party (FDP) – despite appearing as a free rider within its own national governmental coalition – on the premise that the law could undermine Europe's competitiveness and threaten the security of supply chains. This caused Germany to abstain from voting on the law, triggering a domino effect, including a noticeable additional abstention by Italy and France as well as a number of other smaller Member States, which effectively halted the approval of the provisional agreement by the Council. Additionally, France did not firmly support the co-legislators' text, even suggesting an increase in the threshold for in-scope companies from 500 to 5,000 employees.

The Council's deadlock led the Belgian presidency to delay the vote twice in hopes of gaining last-minute support for the co-legislators' proposal. However, on February 28, 2024, the EU ambassadors in COREPER could not secure enough support from EU capitals for the provisional agreement.

Some of the Consequences of Failed Negotiations

This law is of fundamental importance, not only for the game-changing provisions it would have introduced on its own, but also because it could have established consistency across different EU laws providing for ESG related obligations, including the Corporate Sustainability Reporting Directive. The CSDDD would have also served, in some ways, as an umbrella legislation for the due diligence obligations introduced by some recent sector-specific regulations, such as the EU Deforestation Regulation or the EU Battery Regulation. The failure to approve the law would mean losing the guiding role that the CSDDD could and should have played.

The same applies at the national level, where, on one hand, some Member States were awaiting the adoption of the CSDDD to introduce national ESG due diligence legislations, and on the other hand, some countries already equipped with such legal frameworks, such as France or Germany, would have seen their legislative regimes being impacted by the EU directive. Interestingly, those two are also countries whose abstention prevented the required majority to be reached, hampering thereby the creation of an EU level playing field on ESG due diligence requirements.

ESG due diligence obligations first arose with the **French Law of Vigilance** *(Loi de Vigilance – Loi n° 2017-399 du 27 mars 2017 relative au devoir de vigilance des sociétés mères et des entreprises donneuses d'ordre*), as France was the first EU Member State to require companies to implement instruments capable of monitoring supply chain risks, following in particular the Rana Plaza disaster in 2013.

Since the entry into force of that law, in-scope businesses have deployed strong preventive measures against violations of human rights, fundamental freedoms, personal health and safety, and environmental regulations. The CSDDD would have the benefit to more accurately define the nature of the obligations and the level of control required over the supply chain, given the uncertainty of the French Law of Vigilance in that regard. It would also enhance visibility and foreseeability for corporations currently facing NGOs' claims before French courts. Additionally, the current reduced thresholds of the CSDDD would make accountable not only companies counting at least 5,000 employees in France or 10,000 worldwide (i.e., the current Loi de Vigilance threshold), but also every player acting in the supply chain to comply with the highest ESG standards.

The German Act on Corporate Due Diligence Obligations in Supply Chains (*Lieferkettensorgfaltspflichtengesetz*) has also been in effect since January 2023. Germany's opposition to the CSDDD centers on fears that the directive will put businesses under extra bureaucratic strain and open up liability risks due to an overly wide definition of supply chains. There are indeed noticeable differences with the proposed EU directive, which would ultimately have primacy over existing national legislations. First, the scope of the CSDDD is broader as it not only aims to mitigate the negative impact of companies on human rights, but also on the environment. Also, triggering thresholds of the CSDDD are lower. While the German law applies (from 2024) to enterprises with 1,000 or more employees in Germany, the CSDDD would already trigger obligations for EU companies and parent companies with 500 employees or more, and a global turnover above €150 million. Moreover, even though due diligence obligations apply to the entire supply chain in the German law, it limits the direct duty of care to the company itself and its direct suppliers. By contrast, the CSDDD does not differentiate between direct and indirect suppliers. Under the German law, enterprises outside the scope of application are not subject to fines or legal obligations. The EU directive will include administrative sanctions and civil liability, reinforcing the access to justice of persons affected.

Anticipated Next Steps

Belgium, currently holding the presidency of the Council, will assess if it is possible to address EU Member States' concerns in consultation with the European Parliament. Among the possible scenarios to "save" the law is the endorsement of the provisional agreement by the Council by March 7. If the agreement is not endorsed by that date, the most likely scenario is that work on the law will continue under the next political mandate of the European Parliament, making the adoption of the law, at least in its current form, more than uncertain. In the absence of formal adoption, the two institutions might reopen negotiations in the next term, further amend the text, and potentially cast doubts on the adoption itself.

In mid-March, the Conference of Committee Chairs (CCC) will convene a meeting to discuss the status of remaining files and the outlook for the new term. The last session of the European Parliament before elections is scheduled for April 22-25. Files not approved by the end of this mandate will be carried over to the next one. However, their reconsideration depends on the legislative stage they have reached, particularly on the side of the European Parliament.

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