Cefic views on the Corporate Sustainability Due Diligence Proposal

The European chemical industry is an industry of industries – providing building blocks on which modern societies are built, our materials are found in all industries, from agriculture to construction, food and beverages, energy, healthcare, machinery, textiles, hospitals and transportation. Employing 1.2 million workers and with €499 billion in turnover, the European chemical industry is a wealth generating sector and a major contributor to building a sustainable future for Europe.[1]

As recognized by the European Commission's proposal on Corporate Sustainability Due Diligence (hereafter referred to as "Proposal") EU companies operate in complex value chains and an increasing number are voluntarily using value chain due diligence to identify adverse risks and build resilience. Within the context of this Proposal, it is important to consider credible industry specific efforts and to collaborate on delivering intended objectives.

Cefic membership are committed to the promotion of Responsible Care and Safety in Europe and globally – beyond legislative and regulatory compliance – to safely manage chemicals at all stages of the value chain.[2] The initiative represents a key role in the industry's drive for sustainability and includes both products and industrial processes.[3] Additionally, the Safety and Quality Assessment for Sustainability (SQAS) database supports sustained dialogue between chemical companies and their Logistics Service Providers (LSPs).[4] This tool is used to audit the performance of logistic service providers in the value chain based on a range of sustainability criteria in line with the Proposal.

The Commission Proposal identifies that voluntary actions have not resulted in substantial improvement of due diligence across sectors and seeks to address the harmonization challenges stemming from individual Member State actions. Cefic understands the intention of the Proposal while cautioning that the current draft would significantly increase ESG litigation risk in Europe. The objective of this Proposal should not be to create new substantive standards for companies, but to distinguish which are considered critical and request company compliance and due diligence to ensure them.

While there is opportunity to simplify the Directive proposal to elicit meaningful transparency (generation of reliable, comparable and consistent information), there is also an urgent need to clarify key elements and definitions (as has also been raised by the Regulatory Scrutiny Board[5]). Such amendments will ensure harmonized interpretation, transposition and enforcement across the EU27.

[1] 2022 Facts and Figures of the European Chemical Industry
[2] Responsible Care – An ethical framework towards safe chemicals management and performance excellence
[3] Chemicals safety in the value chain: How the European chemical industry manages safe use of chemicals
[4] Safety and Quality Assessment for Sustainability – Cefic
[5] Regulatory Scrutiny Board: Opinion #1 and Opinion #2

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Cefic Recommendations Summary:

1. Core definitions are overly broad which leads to legal uncertainty and fragmented application. A review of key concepts, and subsequent transposition, is necessary to ensure intended objectives are met. (Issues 1, 5, 6, 8, 9)
2. Corporate groups with multiple companies meeting the proposed thresholds should be able to demonstrate compliance in a consolidated manner. (Issue 2)
3. Sanctions imposed due to non-compliance with the due diligence obligations must be proportionate and consider KPIs beyond a company's turnover. (Issues 3, 4, 7)

Generally, Cefic stresses the importance of coherence and consistency with existing and forthcoming reporting requirements, measures and definitions set out in related legislation (i.e., NFRD, CSRD, SFDR) and international standards (i.e., GRI, IFRS). Failure to streamline regulatory reporting frameworks leads to overlapping, potentially inconsistent or contradictory legislation which may result in non-value adding or duplicative obligations on companies.

Please refer to the accompanying Technical Annex for a more detailed description and recommendations.

Cefic continues to support the European Commission and is committed to contributing to the development, analysis and review of all components of the Corporate Sustainability Due Diligence Proposal with evidence-based recommendations.

Technical Annex

<table>
<tr><th colspan="2">Issue I: Clarity of due diligence obligations [Articles 3 (f)(g)(o), 7, 8 and 25]</th></tr>
<tr><td colspan="2">Due diligence perimeters must be clear and correspond to what companies can control. Key definitions are overly broad and expectations for companies are unclear. The current proposal involves considerable complexity in practical terms and proportionality must be considered.</td></tr>
<tr><td>Proposed Solution

1) Recommendation to revise Article 3(f) to read: “means a direct business relationship which is lasting in view of its intensity or duration, and which does not represent a negligible or merely ancillary part of the supply chain”. Further clarification on “intensity” and “duration” is needed.
2) The downstream value chain should not be included in the scope of the current legislation. As a result, due diligence requirements and a liability clause should only be introduced on the condition that only controlled entities and first-tier suppliers are in scope.
3) For Article 3(g) a stepwise approach to implementation with clearly defined parameters, starting with addressing the upstream supply chain, then review and consideration of incorporation of the downstream value chain is recommended.
4) The current definition of “director” could potentially capture any management position, as such, a recommendation to revise to read: “a person appointed or elected to sit on a board that manages the affairs of a corporation or other organization by electing and exercising control over its officers”.</td>
<td>Justification

The proposed due diligence requirements cannot be reasonably implemented on the downstream value chain as companies cannot control all participants operating in their value chain (despite contractual clauses and codes of conduct). The circumstance that the downstream value chain is not under companies’ control should be more carefully considered throughout the proposal.

Given the proposed enforcement mechanisms it is necessary to clearly define the perimeter of due diligence obligations. The boundary of the value chain should be defined relative to an undertaking’s material risks, opportunities and impacts.

Current Member State initiatives (i.e., French[6] and German[7] laws) utilize the term “supply chain”. As such, it is reasonable to start with supply chain, with a view to value chain expansion subject to further analysis.

Considering the consequences with regard to liability in relation to the position of “director”, there should be legal certainty about what position is meant.

The formulation of Article 25 is imprecise as it refers to undefined and broad terms (i.e., sustainability). This does not provide legal certainty and will lead to fragmentation of the EU Single Market as each Member State will interpret such terms in different ways. Clarifying the scope will address such challenges.</td></tr>
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[6] French Corporate Duty of Vigilance Law, 2017
[7] German Supply Chain Act, 2021

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<tr><th colspan="2">Issue 2: Application of due diligence obligations to companies pertaining to the same group [Articles 5, 11, 15, 17 and 25]</th></tr>
<tr><td colspan="2">Due diligence obligations are framed as applying to each individual company caught by the thresholds. There is no explicit reference for an option to demonstrate compliance in a consolidated manner. This is critical for corporate groups with multiple companies meeting thresholds.

With directors’ duty of care, it is unclear what this means for subsidiaries that are part of their corporate group’s strategy.</td></tr>
<tr><td>Proposed Solution

1) Recommendation that Article 11 provides the possibility for companies in third countries to refer to global reporting. The content and format of the reporting with regards to due diligence, set by the delegated acts under Article 11(2) should be fully aligned with the content and format required by the CSRD. Additionally, the reporting should not be linked to financial reporting for non-EU companies.
2) Companies determine fiscal years in different ways – the reporting obligation should allow for companies to report on due diligence within 6 months from the end of their Fiscal Year.
3) Allowance could be made for consolidated group compliance with the addition of: “For the purposes of paragraph 1, Member States shall ensure that where several companies within a single economic entity (a group) meet the threshold under point (a), compliance with the obligations set out in art. 4(1) can be achieved in a consolidated manner” in Article 2. For consistency, a similar paragraph should be added to Article 4.
4) Same consolidation is needed for the specific obligation regarding climate change (Article 15).</td>
<td>Justification

Due diligence processes are driven at corporate level, and in line with current CSRD discussions, consolidated sustainability reporting at parent company level of subsidiaries established in the EU and in third countries should be promoted.

The proposed changes would enable companies to fulfil their obligations, while promoting a high compliance rate and efficient use of resources for companies belonging to the same corporate group.</td></tr>
<tr><th colspan="2">Issue 3: Fair and proportionate public enforcement mechanism [Articles 18, 20]</th></tr>
<tr><td colspan="2">The Directive proposes overly broad descriptions of companies’ obligations – legislation must instead be clear and predictable (legal certainty) given non-compliance may lead to substantial fines.

There is no clear correlation between a company’s turnover and the severity of a human rights or environmental impact it might cause while operating (contrary to domains such as anticorruption or antitrust where the uncompliant behavior is directly related to the intention of generating a profit).</td></tr>
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Sanctions for non-compliance must be reasonable and proportionate and should be proportionate with the severity of the non-compliance and of the damage (if any).

Proposed Solution	**Justification**
1) Recommended that pecuniary sanctions should only be imposed after a company has ignored a formal instruction by the Supervisory Authority to comply with a specific due diligence obligation. Moreover, they should not be based on the company's turnover but capped. 2) Dissuasive sanctions which are not based on the company's turnover should be considered.	Defining pecuniary sanctions based solely on a company's turnover can contravene the principle of proportionality between penalties and offences as well as the principles of justice and fairness of sanctions.

Issue 4: Proportionate private enforcement mechanism [Article 22]
The German and Norwegian frameworks have omitted civil liability altogether because existing tort law allows for damaged parties to seek compensation. Article 22 seeks to bring harmonization by establishing civil liability in relation to Articles 7 and 8 but risks the objective of harmonization. For instance, it does not indicate which standard of proof (i.e., intentionality, gross negligence, etc.) needs to be part of the legal assessment. This risks inconsistency across the EU if implementation of the provision is left to the legal systems of the Member States. There is also lack of clarity in the connection between the breach of certain due diligence obligations (Articles 7 and 8) and the damage that has occurred. Further comments (Article 22): - **Paragraph 2** attempts to exclude liability for damages caused by indirect business relationships but uses complex legal drafting that requires clarification. - It is unclear what is meant in **Paragraph 3** by the supposed establishment of a joint liability without clarifying what the company can ask from the entities that actually caused the damage (right to redress). - It is unclear what is meant in **Paragraph 5** by the supposed mandatory application of EU (transposed) law to a case where foreign law would apply. An expansion of the jurisdiction of Members States' courts beyond EU's territorial limits does not appear to be legally sound; there is a need to clarify the link with Brussels I and Rome II regulations.

Proposed Solution	**Justification**
1) Liability should only be considered in relation to damage actually caused by companies in accordance with existing Member State tort law. 2) The Proposal should omit paragraph 5 as drafted as Member States' legal systems already contemplate when their jurisdiction would apply in certain cases.	The existence of a business relationship should not be sufficient for the imposition of liability as companies cannot control the behavior of third parties. A company's degree of leverage (and potential leverage) vis-à-vis its business partners may vary widely. Article 22 does not adequately consider this and opens opportunity for forum shopping.

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<tr><th colspan="2">Issue 5: Clarification on the withdrawal of public support [Article 24]</th></tr>
<tr><td colspan="2">Pursuant to Article 24, any sanction imposed for non-compliance would systematically prevent a company from getting any public support with no time limitation, relation with the nature or severity of the breach and no definition/limits of “public support”.

Member State responsibility in defining “public support” and therefore the sanctions imposed for non-compliance would give rise to fragmented implementation and would be detrimental to the creation of a level playing field.</td></tr>
<tr><td>Proposed Solution

1) A clear definition of “public support” should be provided by the Proposal.</td><td>Justification

When a Supervisory Authority fines an entity, the matter should be closed (ne bis in idem). In addition, there is lack of a proportionality assessment, no limitation in time and no possibility to appeal, thereby violating fundamental principles of law.</td></tr>
<tr><th colspan="2">Issue 6: Creating and maintaining proportionate supervisory enforcement culture [Articles 9, and 17 to 19]</th></tr>
<tr><td colspan="2">Contrary to Article 17(1) – competence of supervisory authorities limited to the due diligence obligations in articles 6-11, as well as the obligations in Article 15(1) and (2) regarding climate plan and carbon reduction targets – the wording of Article 19 concerning "substantiated concerns" that can be brought before a Supervisory Authority is unlimited and refers instead to all breaches of the Proposal. This means that any person or group could bring a case before a Supervisory Authority also regarding the rules on directors’ duties (articles 25-26), and directors’ variable remuneration (Article 15(3)). There is also potential for simultaneous proceedings under both mechanisms (civil and private) for the same issue, and it is unclear how this will be managed.

The scope of Article 9 – “impacts with respect to their own operations, the operations of their subsidiaries and their value chains” – differs from the one of due diligence, which refers to “impacts arising from their own operations or those of their subsidiaries and, where related to their value chains, from their established business relationships” (Article 6).

It is also unclear which parts of the Proposal the Supervisory Authority is intended to have the competence to enforce.</td></tr>
<tr><td colspan="2">Regulatory Scrutiny Board

The necessity to regulate directors’ duties on top of due diligence requirements is unclear, considering that the due diligence option already requires risk management and engagement with stakeholders’ interests.</td></tr>
<tr><td>Proposed Solution

1) Competence of the Supervisory Authority and scope of Articles 9 and 19 should be limited to the due diligence obligations set out in articles 6-11 and should not extend to controlling “compliance” with Article 15.</td><td>Justification

The mechanism in the proposed Directive is open to abuse by the submission of a deliberately overwhelming number of claims/concerns. Even if claims/concerns are ultimately determined not to be legitimate or substantiated, it takes time and resources to reach that outcome.</td></tr>
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<tr><td>
2) Mechanisms – possibly inspired by the Plaumann formula – to filter out frivolous/unjustified claims at an early stage are recommended. It is recommended to add a specification that concerns can only be submitted by those that allege to have suffered damage as a direct, causal result of a companies' failure to comply with the obligations under the Proposal (as transposed in national legislation). Some criteria (i.e., legitimate interest) to be fulfilled – at least by legal persons – should be envisaged for those who want to submit claims/concerns.
3) Mirroring the scope of due diligence in related articles (drafting alignment), i.e., matching the scope of the complaints procedure to the one of due diligence and matching exclusions of liability for damages caused by indirect business relationships in civil procedures. Currently this does not apply to fines imposed by the Supervisory Authority, but it should. There is no justification for deviating from the scope of civil liability and managing the additional risk would be unduly burdensome for companies.

As well the point also made regarding civil claims – only concerns that have a genuine link with the EU can be brought before a supervisory authority.
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<tr><td colspan="2">Issue 7: Avoiding unintended consequences in case an adverse impact occurs [Articles 7(5), 8(6)]</td></tr>
<tr><td colspan="2">The proposed measures seem excessive and may be counterproductive. Requiring Member States to provide for the option to terminate the business relationship in contracts governed by their laws is contrary to the principle of proportionality as it not only governs due diligence principles but also Member States' general contract law principles. This seems too far-reaching in light of the Proposal's objectives. Indeed, in some cases refraining from "entering into new or extending existing business relations with the partner in connection with or in the value chain of which the impact has arisen" will have no influence on the proper prevention or remedial of the adverse impact.</td></tr>
<tr><td>Proposed Solution

1) To a certain extent, prevention and/or remedial action can be better achieved by</td><td>Justification

Terminating the business relationship is a drastic measure that is only adequate in specific</td></tr>
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<tr><td>extending these business relations as it would give more leverage to the company. This leverage may in turn be used to compel the business partner to better comply with due diligence.[8] [9]</td><td>situations (i.e., where the company lacks leverage to prevent or mitigate adverse impacts and is unable to increase its leverage).10

Furthermore, the mandatory measures set out in articles 7(5) and 8(6) may be found in breach of articles 16 (Freedom to conduct a business) and 52 (Scope of guaranteed rights) of the EU Charter of Fundamental Rights.</td></tr>
<tr><td colspan="2">Issue 8: Precision of prohibitions and violations to ascertain duties needed [Articles 3(b)(c) and 15, and Annex Parts 1-2]</td></tr>
<tr><td colspan="2">Obligations and prohibitions listed in the Annex and enshrined in applicable international conventions must be further clarified. The way they are designed in the Proposal generates legal uncertainty, leaving wide room for interpretation of many concepts contained therein, and contravenes the principle of legality since they are linked to the imposition of sanctions.

Furthermore, these obligations may be implemented in various ways by different State Parties. Where international conventions are implemented in national law, compliance or violation by a company must be interpreted according to national law. The latter may not have ratified or be a Party to all these international conventions (i.e., German law), thus leading to legal uncertainty for operators on whether to apply international standards or local law when implementing due diligence.

It is unclear what is meant in Article 15(1) by the supposed creation of a standard of results through the wording “to ensure”.</td></tr>
<tr><td colspan="2">Regulatory Scrutiny Board

There must be precision in which selected international environmental conventions should be included in the material scope of the due diligence obligations and why. Additionally, it is necessary to assess how EU corporate sustainability governance rules would fit with the different corporate governance models existing in the EU, given the national focus of company law.</td></tr>
<tr><td>Proposed Solution

Recommendation to refine certain provisions:

1) Article 3(b): “‘adverse environmental impact’ means an adverse impact on the environment resulting from the violation of one of the prohibitions and obligations pursuant to the international environmental conventions listed in the Annex, Part II, which has been codified as applicable to private entities in the national provisions</td><td>Justification

It is important that any obligations imposed on companies is consistent with Member State action and legislation implementing the international conventions referred to in the Annex.

This Annex risks mixing the roles of states and companies. Currently, obligations related to international conventions are imposed on companies regardless of national</td></tr>
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[8] UNGP, Commentary under Principle 19, pages 21-22

[9] Section 4.8 “Leverage and the ability of individual companies” (74-77) and Section 7 “Conclusions: Market Practices” (151-155), Study on due diligence requirements through the supply chain, 2021.

[10] Ibid, UNGP.

implementing one of those prohibitions and obligations". 2) Article 3(c): "'adverse human rights impact' means an adverse impact on protected persons resulting from the violation of one of the rights or prohibitions listed in the Annex, Part I Section 1, as enshrined in the international conventions listed in the Annex, Part I Section 2, which has been codified as applicable to private entities in the national provisions implementing one of those prohibitions and obligations". 3) Annex Part II §1: "1. Violation of the obligation to comply with the necessary measures adopted by States in relation to the use of biological resources in order to avoid or minimize adverse impacts on biological diversity, in line with Article 10 (b) of the 1992 Convention on Biological Diversity (…)". 4) Annex Part I §7, it should be added: "a 'fair wage' shall mean a wage that meets or exceeds the minimum wage in accordance with applicable law". This is also in line with the German law on due diligence where they have incorporated this clarification. 5) Annex Part I §17 ("prohibition of withholding an adequate living wage"), §18 ("prohibition of causing any measurable environmental degradation (…)"), and §19 ("prohibition to unlawfully evict or take land, forests and waters when acquiring, developing or otherwise use land, forests and waters (…)") should be deleted or realigned with actual requirements of applicable international conventions. 6) Annex Part I §21 should be deleted.	implementation. For instance, the measures under Annex Part II §1 are to be adopted by states to regulate their territory such as urban planning, natural site protection, permitting procedures subject to environmental assessment, etc. A company cannot be expected to take such measures. Some of the obligations under Annex Part I are not per se obligations contained in the referenced international documents but rather attenuated interpretations of existing international documents. The relevant paragraphs are therefore deprived of a clear legal basis. Many notions in the Annex (i.e., 'fair wage') need to be clearer and more specific: rule of law requires that legislation be intelligible, clear and predictable, enabling companies to understand what their due diligence obligations are. As to Annex Part I §18, this prohibition does not flow from the reference provisions (Article 3 of the UDHR, art. 5 of the ICCPR and Article 12 of the ICESCR). Moreover, the subject matter (violations of prohibitions and objectives included in environmental conventions) is already covered in Annex Part II. Specifically for "deforestation", it is subject to a separate legislative proposal. Annex Part I §21 defeats the purpose of listing the prohibitions and objectives that are in scope of the Proposal, generating legal uncertainty.
Issue 9: Application of Paris Agreement goals to individual companies (Articles 15 and 17)	
Recalling the Commission assessment and proposals[11] different measures are necessary in all sectors to meet the 2030 and 2050 climate targets. It is unclear whether greenhouse gas emission reduction measures are appropriate for this proposal given the proposal does not refer to the EU Treaty legal basis on environmental policy and that the Commission has taken a different approach with the EU Climate Law and Fit for 55 Package, inviting the private sector to engage in sector-specific roadmaps to plan their transition towards achieving the Union's climate-neutrality objective by 2050.	

[11] European Climate Law and "Fit for 55" Package

Proposed Solution	Justification
1) Refinement of Article 15 (1) to read: "[…]shall adopt a plan aiming to make the business model and strategy of the company compatible with applicable law on climate change mitigation […]". 2) In Article 17(1), the words "and Article 15(1) and (2)" should be deleted.	Building on the content in Issue 8, if the Paris Agreement relies on the Member States to define the way final climate change goals will be achieved in their territory, it is not a correct legislative approach to overrule the State authority and require companies to take the measures regardless of the State regulations. Focusing on the purpose according to Article 15 (i.e., combating climate change), no reference to a sustainable economy is required. Since it will be a challenge for companies to provide robust quantitative evidence for their plans to be aligned with global or regional goals, given the complexities of breaking down such goals to sectors and companies and respective initiatives (i.e., Science-Based Targets initiative) being in a too early stage to be used, the plans should focus on measures taken towards alignment.

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About Cefic

Cefic, the European Chemical Industry Council, founded in 1972, is the voice of large, medium and small chemical companies across Europe, which provide 1.2 million jobs and account for 15% of world chemicals production.