

Government Analytica Legislation/Regulation Analysis

European Union Corporate Sustainability Due Diligence Directive (CSDDD)

Purpose of the Legislation/Regulation

To mandate large companies operating in the EU to conduct human rights and environmental due diligence in their operations and across their supply chains.

Key Legislation/Regulation Points

- Establishes minimum due diligence standards for EU Member States to transpose into national law.
- Requires companies to integrate due diligence into policies and risk management systems.
- Mandates periodic assessments to identify and prioritize potential adverse impacts.
- Companies must take measures to prevent, mitigate, and remediate identified adverse impacts.
- Requires the establishment of notification and complaints procedures.
- Companies must monitor and report on the effectiveness of their due diligence policies.
- Introduces obligations to combat climate change through the adoption of a climate transition plan.
- Applies to large EU and non-EU companies meeting specific employee and financial thresholds.

Next Steps

- EU Member States must transpose the Directive into national law within two years.
- Companies in Group 1 (over 5000 employees, EUR 1500 million turnover) must comply by 2027.
- Companies in Group 2 (over 3000 employees, EUR 900 million turnover) must comply by 2028.
- Companies in Group 3 (over 1000 employees, EUR 450 million turnover) and franchised companies (over EUR 80 million turnover) must comply by 2029.
- The EU Commission will assess the potential application of due diligence requirements for financial institutions by May 2026.

Summary

The CSDDD aims to harmonize due diligence practices across the EU, fostering responsible business conduct and protecting human rights and the environment. It also provides a framework for continuous improvement and stakeholder engagement, ensuring that companies take proactive measures to address and mitigate adverse impacts.

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The Corporate Sustainability Due Diligence Directive (CSDDD) aims to mandate large companies operating within the EU to incorporate human rights and environmental due diligence into their operations and supply chains. The directive seeks to harmonize due diligence requirements across EU Member States, setting minimum standards to ensure responsible business conduct. This legislation is intended to level the playing field for businesses within the EU market, requiring them to identify, address, and mitigate adverse human rights and environmental impacts.

Key Legislation/Regulation Changes

1. Integration of Due Diligence into Policies and Systems

- **Article 5:** Companies must adopt policies to ensure risk-based human rights and environmental due diligence.
- Integrate due diligence policies and processes across the company and risk management systems.

2. Identification and Assessment of Adverse Impacts

- **Article 6:** Companies must map their operations and activities to identify adverse impacts.
- Conduct periodic assessments using internal and external information to identify and prioritize impacts based on severity and likelihood.

3. Prevention and Mitigation of Adverse Impacts

- **Articles 7 & 8:** Implement measures to prevent, mitigate, and remediate adverse impacts.
- Develop corrective action plans, participate in multi-stakeholder initiatives, and seek contractual assurances from business partners.
- Provide support to SMEs involved and ensure meaningful stakeholder engagement throughout the due diligence process.

4. Establishment of Notification Mechanisms and Complaints Procedures

- **Article 9:** Set up accessible notification mechanisms for stakeholders and a transparent procedure to address complaints, preventing retaliation.

5. Monitoring the Effectiveness of Due Diligence

- **Article 10:** Periodically assess the effectiveness of due diligence policies and processes, and the measures taken to address adverse impacts.

6. Public Communication on Due Diligence

- **Article 11:** Companies must report on their due diligence practices annually, in compliance with the Corporate Sustainability Reporting Directive (CSRD).

7. Combatting Climate Change

- **Article 15:** Adopt and implement climate transition plans aligned with the Paris Agreement, including specific targets and actions for decarbonization.

Scope of the Directive

- **Group 1:** EU companies with > 1000 employees and > EUR 450 million turnover.
- **Group 2:** Non-EU companies with > 1000 employees and > EUR 450 million turnover in the EU.
- **Group 3:** Franchised companies (EU and non-EU) with > 1000 employees and specific financial thresholds.

Implementation Timeline by Company Size

- The directive will come into force 20 days after publication in the Official Journal of the European Union, with phased compliance based on company size and turnover:
 - 3 years for companies with > 5000 employees and > EUR 1500 million turnover.
 - 4 years for companies with > 3000 employees and > EUR 900 million turnover.
 - 5 years for companies with > 1000 employees and > EUR 450 million turnover, and those with franchising agreements exceeding EUR 80 million.

What to do Next?

For Companies:

1. Assess current capabilities and frameworks for due diligence and risk management.
2. Define roles and responsibilities for environmental and human rights due diligence.
3. Engage stakeholders to shape strategy and grievance mechanisms.
4. Map the value chain to identify potential impacts.
5. Develop and implement a due diligence roadmap aligned with CSDDD requirements.

For Member States:

- Transpose the CSDDD into national law within two years.
- Establish national supervisory authorities to oversee implementation and compliance.

Challenges Companies Face Implementing CSDD Directive

Implementing the Corporate Sustainability Due Diligence Directive (CSDDD) poses several significant challenges for companies. Here are the top five challenges they may face:

1. **Complexity of Supply Chain Monitoring:** Monitoring the entire supply chain for human rights and environmental risks is a major challenge, especially for large multinational companies with extensive and complex supply chains. The directive requires companies to identify, prevent, and mitigate adverse impacts, which involves scrutinizing not just direct suppliers but also indirect suppliers and various stakeholders involved in the production process.
2. **Administrative and Compliance Burden:** The CSDDD introduces new reporting and documentation requirements that significantly increase the administrative burden on companies. Ensuring compliance with these requirements demands substantial resources, including dedicated personnel, updated IT systems, and ongoing training programs. This can be particularly burdensome for companies that already operate under multiple regulatory frameworks.
3. **Legal and Financial Risks:** Companies face heightened legal and financial risks under the CSDDD, including potential civil liability for failing to comply with due diligence obligations. If adverse impacts occur and it is found that the company did not take appropriate measures to prevent or mitigate them, the company could be liable for significant damages. This risk necessitates robust compliance mechanisms to avoid litigation.
4. **Integration with Existing Corporate Governance:** Integrating due diligence into existing corporate governance structures can be challenging. Companies must align their policies and procedures with the directive's requirements, which may involve significant changes to governance frameworks and risk management systems. Additionally, the directive may impact directors' duties and remuneration, adding a layer of complexity to corporate governance.
5. **Economic Impact and Competitiveness:** The increased costs associated with compliance could affect the competitiveness of companies, particularly those operating in high-impact sectors like textiles, agriculture, and mining. Smaller companies within the supply chains of larger entities might also face economic pressures as they strive to meet the due diligence standards imposed on them indirectly.

Addressing these challenges requires companies to adopt proactive strategies, invest in compliance infrastructure, and engage in continuous stakeholder dialogue to ensure they meet the directive's requirements effectively.

8-Ways Companies Can Prepare for CSDDD

To meet the requirements of the Corporate Sustainability Due Diligence Directive (CSDDD), companies should organize themselves internally through the following steps:

1. Establishing a Cross-Functional Due Diligence Team

Create a dedicated team that includes members from various departments such as legal, compliance, procurement, HR, and sustainability. This team should be responsible for overseeing the implementation of due diligence processes and ensuring compliance with the directive's requirements.

2. Integrating Due Diligence into Corporate Governance

Ensure that due diligence is embedded into the company's governance framework. This includes updating the company's policies and risk management systems to incorporate human rights and environmental

considerations. Board members should be involved and held accountable for due diligence performance, aligning their responsibilities and remuneration with sustainability targets.

3. Conducting Thorough Supply Chain Mapping and Risk Assessment

Map the entire supply chain to identify potential human rights and environmental risks. This involves collecting detailed information on suppliers and sub-suppliers, assessing risks based on the severity and likelihood of impacts, and prioritizing areas where the risks are highest. Regular assessments and updates should be conducted to maintain an accurate risk profile.

4. Developing and Implementing Policies and Procedures

Formulate comprehensive due diligence policies that define clear procedures for identifying, preventing, mitigating, and addressing adverse impacts. These policies should be integrated into everyday business operations and communicated effectively across the organization. Companies should also establish robust grievance mechanisms to address any complaints related to human rights or environmental issues.

5. Training and Capacity Building

Invest in training programs for employees at all levels to ensure they understand the requirements of the CSDDD and their roles in meeting these obligations. This training should cover the importance of due diligence, the specific processes to be followed, and the tools available to support these efforts. Continuous capacity building is essential to adapt to evolving regulations and practices.

6. Enhancing Stakeholder Engagement

Engage proactively with stakeholders, including employees, suppliers, customers, and affected communities. Meaningful stakeholder engagement is crucial for identifying potential impacts and developing appropriate mitigation strategies. Companies should establish regular communication channels to gather feedback and report on due diligence activities.

7. Monitoring and Reporting

Set up mechanisms for ongoing monitoring and evaluation of due diligence processes. This includes tracking the effectiveness of implemented measures and making necessary adjustments. Companies should also report annually on their due diligence activities, either through existing sustainability reporting frameworks like the Corporate Sustainability Reporting Directive (CSRD) or through dedicated reports.

8. Leveraging Technology and Digital Tools

Utilize digital tools and platforms to streamline due diligence processes. These tools can help with data collection, risk assessment, monitoring, and reporting, making it easier to manage complex supply chains and large volumes of data. Technologies such as blockchain can enhance transparency and traceability across the supply chain.

By following these steps, companies can build a robust internal framework to meet the requirements of the CSDDD, ensuring that they effectively manage human rights and environmental risks and comply with the new regulatory landscape. The CSDDD represents a significant shift towards embedding responsible business practices in EU companies. It is crucial for companies to begin preparing now to meet the directive's requirements and timelines. This directive not only aims to protect human rights and the environment but also to create a consistent regulatory environment across the EU, fostering fair competition and sustainable business practices.

Corporate Sustainability Due Diligence Directive (CSDDD) Implementation Questionnaire Workbook

This questionnaire is designed to help companies assess their readiness to implement the Corporate Sustainability Due Diligence Directive (CSDDD). It includes a self-ranking system for answers, allowing companies to gauge their current compliance status and identify areas for improvement.

Instructions:

- For each question, provide a score based on your current level of compliance.
- At the end of each section, total your scores to get a numerical assessment of your readiness.
- Use the scoring guide provided to interpret your results.

Section 1: Governance and Policy Integration

1. Governance Framework

- Do you have a dedicated team for overseeing due diligence implementation?
 - Score: 0 (No team) | 1 (Ad-hoc team) | 2 (Formal team with defined roles) | 3 (Fully integrated team across departments)
- Have you integrated due diligence into your corporate governance framework?
 - Score: 0 (Not integrated) | 1 (Partially integrated) | 2 (Mostly integrated) | 3 (Fully integrated with board oversight)

2. Policy Development

- Do you have a written policy on human rights and environmental due diligence?
 - Score: 0 (No policy) | 1 (Drafted) | 2 (Implemented) | 3 (Reviewed and updated regularly)
- Are these policies communicated effectively across the organization?
 - Score: 0 (Not communicated) | 1 (Limited communication) | 2 (Regular communication) | 3 (Extensive communication and training)

Total Score for Section 1: _____/12

Section 2: Risk Assessment and Supply Chain Management

3. Supply Chain Mapping

- Have you mapped your entire supply chain to identify potential risks?
 - Score: 0 (Not started) | 1 (Preliminary mapping) | 2 (Detailed mapping) | 3 (Comprehensive mapping with updates)

4. Risk Assessment

- Do you conduct regular risk assessments for human rights and environmental impacts?
 - Score: 0 (No assessments) | 1 (Occasional assessments) | 2 (Regular assessments) | 3 (Comprehensive and ongoing assessments)

5. Prioritization and Mitigation

- Do you have processes to prioritize and mitigate identified risks?
 - Score: 0 (No processes) | 1 (Basic processes) | 2 (Developed processes) | 3 (Fully implemented and effective processes)

Total Score for Section 2: _____/12

Section 3: Stakeholder Engagement and Grievance Mechanisms

6. Stakeholder Engagement

- Do you engage with stakeholders to identify and address due diligence issues?
 - Score: 0 (No engagement) | 1 (Limited engagement) | 2 (Regular engagement) | 3 (Extensive and effective engagement)

7. Grievance Mechanisms

- Do you have accessible grievance mechanisms in place for stakeholders?
 - Score: 0 (No mechanisms) | 1 (Basic mechanisms) | 2 (Developed mechanisms) | 3 (Fully implemented and widely accessible)

Total Score for Section 3: _____/6

Section 4: Monitoring and Reporting

8. Monitoring Effectiveness

- Do you regularly monitor the effectiveness of your due diligence processes?
 - Score: 0 (No monitoring) | 1 (Basic monitoring) | 2 (Regular monitoring) | 3 (Comprehensive and ongoing monitoring)

9. Public Reporting

- Do you publicly report on your due diligence activities?
 - Score: 0 (No reporting) | 1 (Occasional reporting) | 2 (Regular reporting) | 3 (Extensive and detailed reporting)

Total Score for Section 4: _____/6

Section 5: Climate Change and Sustainability Goals

10. Climate Transition Plan

- Have you adopted and implemented a climate transition plan in line with the Paris Agreement?
 - Score: 0 (No plan) | 1 (Drafted) | 2 (Implemented) | 3 (Reviewed and updated regularly)

11. Sustainability Targets

- Do you have clear, time-bound sustainability targets supported by key actions?
 - Score: 0 (No targets) | 1 (Basic targets) | 2 (Developed targets) | 3 (Fully implemented and tracked targets)

Total Score for Section 5: _____/6

Scoring Guide

- **0-10:** High risk of non-compliance. Immediate action is required to start implementing due diligence processes.
- **11-20:** Moderate risk. Some elements of due diligence are in place, but significant improvements are needed.
- **21-30:** Low risk. Due diligence processes are well-developed but require fine-tuning and ongoing monitoring.
- **31-42:** Compliant. Robust due diligence processes are in place and effectively managed.

Overall Total Score: _____/42

Use this questionnaire to as a simple tool identify gaps in your current processes and develop a plan to address them, ensuring compliance with the CSDDD.