

BOARD AGENDA

GOVERNANCE | STRATEGY | RISK | ETHICS

[Home](#) [NEWS](#) [INSIGHT](#) [COMMENT](#) [INTERVIEWS](#) [CAREER](#) [RESOURCE CENTRE](#) [EVENTS](#) [SEARCH BY TOPIC](#)

INSIGHT: CORPORATE SUSTAINABILITY DUE DILIGENCE

Steps to a sustainable supply chain



by **AMY WADDINGTON**

The clock has started ticking on the implementation of the EU’s Corporate Sustainability Due Diligence Directive.



Image: metamorworks/Shutterstock.com

SAVE ☆

The EU Corporate Sustainability Due Diligence Directive (CS3D) will introduce transformative obligations on certain EU and non-EU companies with respect to due diligence and strategic standards on human rights, environment and climate change.

The directive represents a step change on ESG in terms of legal analysis and risk, and provides a new baseline for previously fragmented laws, rules, recommendations and voluntary standards across the EU, with potential financial penalties extending to 5% of a company or group's net worldwide turnover.

The directive represents a step change on ESG in terms of legal analysis and risk.

CS3D entered into force on 25 July 2024: member states have two years to implement it into national legislation ahead of it applying to the first "in-scope" companies from 2027. CS3D will apply to companies incorporated in the EU with more than 1,000 employees and a net worldwide turnover of more than €450m (£378m); and to non-EU companies with an annual net turnover of more than €450m in

the EU. The European Commission expects this to translate to approximately **6,000 EU and 900 non-EU companies** in scope, **relative to the 50,000** expected to be caught by the EU's Corporate Sustainability Reporting Directive (CSRD).

Regulated financial undertakings are subject to slightly modified rules. Small and medium-sized enterprises may be engaged as part of the supply chains of larger companies. In certain circumstances, the in-scope criteria also extends to companies with franchising or licensing agreements, as well as ultimate parent companies.

Green legislation

CS3D sits with CSRD as the central incoming legislation of the **European Green Deal**. CSRD focuses on positive disclosure across a range of ESG metrics—aiming to improve the quality of sustainability reporting relative to the previous regime (the EU Non-Financial Reporting Directive), including through third-party auditing assurance requirements.

The CS3D has a more litigious subtext, driving greater corporate responsibility and accountability through due diligence and remedial obligations across a company's entire supply chain. In addition, CS3D will require in-scope companies to disclose a climate-related transition plan (CTP), including decarbonisation and emissions targets details by reference to specific time periods.

The CS3D has a more litigious subtext, driving greater corporate responsibility and accountability.

Supply chain related obligations under CS3D are to adopt and implement effective due diligence policies for identifying, preventing, mitigating and ending potential and actual "adverse impacts"

on human rights and environmental matters within companies' own operations, those of their subsidiaries and across their "chain of activities".

The latter extends to the activities of business partners upstream (for example, provision of goods and/or services by the relevant company) and downstream (for example, distribution, transport and storage of a product on a company's behalf).

"Adverse" human rights and environmental impacts are defined by reference to a list of legal prohibitions annexed to CS3D, including forced or child labour, inadequate workplace health and safety, and prohibited pollution.

Where potential or actual adverse impacts are identified, CS3D specifies response steps, including a notification mechanism and complaints procedure for those affected, and legitimate representatives of such persons (for example, NGOs or trade unions).

Actions to take now

Companies within scope need to start developing new processes to facilitate and support compliance, including engagement with stakeholders and reviewing procurement policies and practices. Companies not in scope should be aware of any potential indirect impact if, for example, they are **suppliers to a company that is in scope**.

The CTP obligations under CS3D aim to ensure that a company's business model and strategy are compatible with limiting global warming to 1.5°C in line with the Paris Agreement and the EU's objective of achieving climate neutrality by 2050.

These requirements have been influenced by the **global rise in climate change litigation**, in particular, the *State of the Netherlands v Urgenda Foundation (2019)* – the first ever ruling ordering a government to set more ambitious climate targets; and *Milieudefensie et al v Royal Dutch Shell plc (2021)* (currently under appeal, with judgment due in November 2024), in which the Hague District Court ordered Royal Dutch Shell to reduce its emissions by 45% by 2030 across all of its activities.

In making its decision, the Court referred to the IPCC (Intergovernmental Panel on Climate Change), which had identified that emissions must be reduced by net 45% by 2030 and to net zero by 2050 to keep global warming to the Paris Agreement target.

The threat of litigation is expected to support compliance with CS3D, with injured complainants, shareholder activists and investors **buoyed by the rising number of claims** brought for ESG-related failings.

However, CS3D also introduces specific regulatory enforcement mechanics, including a requirement that all EU member states designate a supervisory authority to monitor CS3D compliance and introduce remedial action and/or penalties.

Companies may also be liable for damage caused by failure to prevent or end any adverse impacts in their supply chain. CS3D allows for a five-year period for such claims to be brought and sets out procedural provisions relating to disclosure of evidence, injunctive measures and costs.

Companies should undertake a legal scoping exercise to assess the relevance of CS3D to them (and ideally this exercise would sweep for other ESG regulations to which they may be, or may become, subject; and reflect any relevant and existing reporting data and processes) with a view to creating a roadmap to compliance and highlighting divergent or convergent requirements and equivalence opportunities. From this, effective implementation methods, risk and governance frameworks can develop and core director responsibilities can be managed.

*Amy Waddington is a senior counsel and **key member of Weil's sustainability and ESG advisory group.***



Facebook



Twitter



Google+



LinkedIn



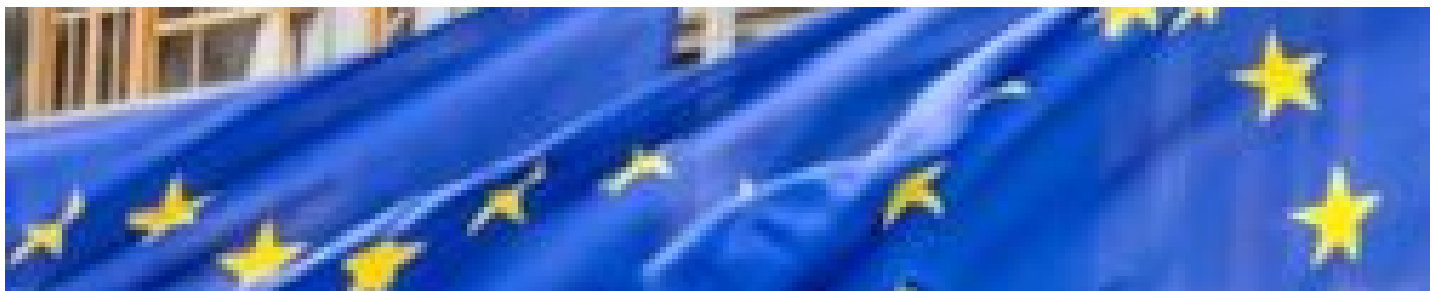
Mail

SAVE ☆

Related Posts

Campaigners protest against EU due diligence proposals

September 7, 2022



Objectors say the directive on corporate sustainability and human rights falls short, while companies criticise the demands it makes.