



Implications of the Upcoming EU Corporate Sustainability Due Diligence Directive

Key takeaways

- In June 2023, the European Parliament adopted its position on the Corporate Sustainability Due Diligence Directive (CS3D), which aims to promote sustainable and responsible corporate behavior. The Directive will now move on to negotiations between Parliament, the Commission, and the Council of the European Union.
- The content of the legislation is not yet final, as it will depend on the outcome of the tripartite negotiations, which are expected to be concluded before the 2024 European elections.
- The proposed directive reinforces previous legislation, such as the Corporate Sustainability Reporting Directive. In practice, companies will be required to prevent, mitigate, and publicly report on the potential and actual impacts of their activities on human rights and the environment throughout their value chain.
- Companies with commercial interests in the European Union (EU) need to monitor the regulatory process closely, build relationships with key audiences within the EU political landscape, as well as prepare and enhance their approach to ESG.

Scope

The European Parliament's position represents the next step for the Directive, which originated in February 2022 in an initial proposal of the European Commission and progressed with the Council of the European Union in December 2022. The Directive now enters the discussion stage with the Commission and the Council, impacting:

- Companies established in the EU, regardless of their sector, with more than 250 employees and global revenues exceeding €40 million, as well as parent companies of subsidiaries in the EU with more than 500 employees and global revenues exceeding €150 million; and

- Non-European companies with a turnover above €150 million, if at least €40 million of these are generated in the EU.

These new obligations would take effect after 3 or 4 years, depending on the size of the company. Smaller organizations may take an additional year to comply with the legislation.

Impact

The European Parliament has proposed that non-compliance with the Directive may result in significant administrative penalties of not less than 5% of the company's worldwide net turnover for the period preceding the infringement. The penalties will be set by the competent authorities of the EU countries. Parliament also included a provision stating that non-compliant third country companies will be banned from public procurement.

Companies are civilly liable and may have to repair damages to affected persons, including compensation or reparations.

Why it matters for non-EU companies

Although the current version of the Directive focuses on companies with substantial operations in the EU, it may have an indirect impact on any company that exports to or has subsidiaries in the EU. Three examples help to explain:

1. **Significant activities in the EU:** If the activities of an exporting company exceed the thresholds (net turnover in the EU exceeding €40 million), the Directive will apply directly to it.
2. **Being part of a value chain:** Companies that are part of a value chain connected to the EU will have to comply with the standards to which the EU-based company they supply is subject (e.g., a supplier of fruit to an EU wholesaler will have to align itself with the standards to which the wholesaler responds).
3. **Companies with an EU subsidiary:** If an EU subsidiary of a parent company is subject to the Directive, the parent could be held responsible for ensuring that its subsidiary complies with the Directive.

Product-specific due diligence requirements will be complemented by horizontal provisions impacting the Directive that will come into force in 2024, such as the veto on products associated with forced labor, along with the veto on products leading to increased deforestation.

There are considerable liability risks for companies doing business in the EU that do not comply with the Directive's standards – they could face lawsuits and reputational damage in case of human rights violations or environmental damage they have caused or contributed to.

How Dentons Global Advisors can help

Negotiations between the EU institutions are expected to run until the end of 2023 or early 2024. Therefore, the Directive starts to apply in all EU countries from 2026 onwards for large EU and non-EU companies.

With a robust team of government relations, ESG and complex communications experts in Brussels, London, Paris, Berlin, Madrid and other European capitals, Dentons Global Advisors can support companies impacted by the increasing regulations in:

- **Monitoring negotiations between the EU institutions** and on key issues such as sanctions and the liability regime, and the extent to which "value chain" obligations will be applied.
- **Developing strategies to engage with key audiences** in the EU institutions and subsequently in the member countries during the process of passing national laws on the subject.
- **Assessing value chains and ESG policies** to prepare companies for the entry into force of the Directive and related regulations by identifying potential risks and gaps in human rights, environmental, and related issues such as deforestation and forced labor.

About Dentons Global Advisors

Dentons Global Advisors is an expert-led advisory firm that provides integrated solutions for clients in an increasingly complex, regulated and interconnected business environment. Comprising Albright Stonebridge Group and a deep bench of communications, public affairs, government relations and strategy consultants, we help clients engage with governments and regulatory bodies, navigate public disclosures and transactions within the private and capital markets, and manage their reputations through critical moments of change, challenge or opportunity. Our relationship with Dentons, the world's largest law firm, means clients can draw upon integrated legal expertise and strategic advisory services when and where they need them.

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