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EU Mandatory Environmental and Human Rights Due Diligence Law – What You Need To Know

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On Wednesday, March 10th, the European Parliament voted by an overwhelming majority for the adoption of a binding EU law that requires companies to conduct environmental and human rights due diligence along their full value chain or face concrete fines, sanctions and/or civil liability.

The European Parliament (adopted by 504 votes in favour, 79 against and 112 abstention) calls for a binding EU law that ensures businesses are held accountable and liable when they harm - or contribute to harming – the environment, human rights and good governance.

Below is a brief overview of the key elements of the report.

Who would fall within the scope of this?

In short, both EU and non-EU businesses:

- large undertakings governed by the law of an EU member state or established in the territory of the EU, regardless of sector of activity and public ownership or control;
- publicly listed and high-risk small and medium-sized undertakings (however, it was recognised that some of these may need less extensive and formalised due diligence processes); and
- undertakings which are established outside the EU but are active in the EU market, regardless of size, operating in high risk sectors.

What is required?

Undertakings must carry out effective due diligence with respect to potential or actual adverse impacts on the environment, human rights and good governance in their operations and business relationships.

Undertakings must first identify and assess, by means of a risk based monitoring methodology that takes into account potential or actual impacts on the environment, human rights or good governance, and whether their operations and business relationships cause or contribute to or are directly linked to any of those potential or actual adverse impacts.

If, as a result of this assessment, an undertaking concludes that it does not cause, contribute to, or that it is not directly linked to any potential or actual adverse impact on the environment, human rights or good governance, it shall publish a statement to that effect. Along with such statement it shall include its risk assessment containing relevant data, information and methodology that led to this conclusion. Such a statement must be reviewed periodically in the

event that new risks emerge or new business relationships are entered into.

Otherwise, undertakings must as part of their due diligence adopt a strategy which:

- specifies the potential or actual adverse impacts on the environment, human rights and good governance in its operations and business relationships;
- map their value chain and, with due regard for confidentiality, disclose relevant information about the undertaking's value chain;
- adopt proportionate policies and measures aimed at ceasing, preventing or mitigating potential or actual adverse impacts on the environment, human rights or good governance; and
- establish a prioritisation strategy on the basis of the UN Guiding Principles on Business and Human Rights.

In terms of an undertaking's business and supply chain:

- due diligence which is proportionate to the risk of potential or actual adverse impacts must be carried out;
- business counterparties must implement environmental, human rights and good governance policies that are in line with such undertaking's due diligence strategy, for example, by means of contractual provisions, the adoption of codes of conduct or certified and independent audits; and
- suppliers and subcontractors must be regularly verified for compliance with their obligations.

Enforcement

One or more national authorities shall be designated responsible for enforcement, with the power to carry out investigations, including with respect to undertakings which have stated that they have not encountered any potential or actual adverse impact on the environment, human rights or good governance.

Penalties

The relevant authority may impose fines calculated on the basis of an undertaking's turnover, exclude undertakings from public procurement, from state aid, from public support schemes (e.g. Export Credit Agencies and loans), seize commodities and other appropriate administrative sanctions.

Undertakings also face civil liability for any harm arising out of potential or actual adverse impacts on the environment, human rights or good governance that they, or any undertakings under their control, have caused or contributed to (whether by way of act or omission).

The European Parliament has also called for additional measures, including a ban on importing products linked to severe human rights violations such as forced or child labour.

What next?

Through this vote, the European Parliament has expressly requested that the body responsible for drawing up proposals for new European legislation (i.e. a directive) – the European Commission - submit without undue delay a directive on such mandatory due diligence. Member states are then to transpose such a directive into national law.

Conclusion

This forms part of a series of initiatives on mandatory environmental and human rights due diligence that have taken place in the context of increasing pressure on businesses and regulators to address ESG concerns. It is envisaged that there will continue to be greater demands for businesses to take concrete steps to address their ESG risks, alongside louder calls for businesses to transition to a low carbon future in a way that is just and inclusive. As such, prudent businesses need to begin working together with their advisers to implement effective measures to identify and manage ESG risks in their business activities and relationships now.