



The Due Diligence Directive enters the final stretch

European Parliament approves final proposal for the Corporate Sustainability Due Diligence Directive

Legal flash

April 26, 2024



➤ On April 24, the European Parliament approved the **final proposal** for the Corporate Sustainability Due Diligence Directive (“CS3D”), which aims to:

- establish a mandatory European standard of business conduct to ensure that companies protect human rights and the environment in their own operations, those of their subsidiaries and across their chain of activities; and
- allow companies to be held liable for damages resulting from violations and abuses.

➤ Final adoption of CS3D is pending approval by the Council, which is expected for May 23.

➤ CS3D, which must be incorporated into national law within two years, will apply gradually to companies according to their profile. **The first ones affected will be largest companies in 2027.**



CS3D is part of the EU's political-legislative framework aimed at establishing specific corporate duties and obligations on environmental, social and governance matters. Among others, CS3D complements the rules on taxonomy, transparency and accountability regarding sustainability (see [Legal Flash | Corporate information on sustainability: CSRD Directive](#)).

The text approved by the Parliament is the result of a legislative process initiated more than two years ago by the European Commission, in which the initial expectations have been lowered. Among the most relevant developments are the following:

- Reduction of the subjective scope (by raising thresholds, by replacing the definition of “value chain” with “chain of activities,” and by limiting the regime applicable to the financial sector).
- Extension of the deadlines for entry into force and implementation.
- Elimination of the internal corporate governance aspects relating to directors—in particular, the rules on their due diligence obligations and variable remuneration linked to climate-related targets.
- Clarification of the grounds for corporate civil liability, which requires fault or negligence and damage to the legal interest of a natural or legal person protected by the regulation. Standing for bringing civil liability actions is also limited.

Objectives

CS3D aims to:

- **improve** corporate governance practices to better integrate risk management and mitigation processes of human rights and environmental risks and impacts, including those stemming from the chain of activities;
- **avoid** fragmentation of due diligence requirements in the single market and create legal certainty for companies and stakeholders as regards expected behavior and liability; and
- **establish** administrative sanctioning mechanisms for non-compliant companies, holding them civilly liable for breach of due diligence obligations under CS3D.

Obligated companies

EU companies

- which, for two consecutive financial years, have (i) more than 1,000 employees; and (ii) a net worldwide turnover exceeding €450 million per year; or
- which, although not exceeding the above thresholds, are the ultimate parent of a group that,



on a consolidated basis, has reached those thresholds for two consecutive financial years; or

- which have entered into (or are the ultimate parent of a group that has entered into) franchise or licensing agreements with independent third-party companies, ensuring a common identity, a common business concept and the application of uniform business methods, provided that (i) the royalties paid for these agreements exceed €22.5 million in the last financial year; and (ii) the company (or the ultimate parent of the group) has a net worldwide turnover of more than €80 million for two consecutive financial years.

Non-EU companies

- which for two consecutive financial years have generated a net EU turnover of more than €450 million per year;
- which, although not exceeding the above threshold, are the ultimate parent of a group that, on a consolidated basis, has reached that threshold for two consecutive financial years; or
- which have entered into (or are the ultimate parent of a group that has entered into) franchise or licensing agreements in the EU with independent third-party companies, ensuring a common identity, a common business concept and the application of uniform business methods, provided that (i) the royalties paid for these agreements exceed €22.5 million in the EU in the last financial year; and (ii) the company (or the ultimate parent of the group) has an annual net EU turnover of more than €80 million for two consecutive financial years.

Exempt companies

EU companies below CS3D thresholds

Although not formally subject to CS3D, the following companies must implement human rights and environmental due diligence and risk management systems:

- Companies subject to sustainability reporting requirements under the **CSRD**. In particular, they must report on management systems regarding risks identified as significant in the mandatory double materiality assessment.
- **Companies, including SMEs, that are part of the chain of activities** of a company falling within the scope of CS3D.

Ultimate parent companies of a group

Ultimate parent companies of a group may be exempt if:

- their **main activity consists of holding shares** in operational subsidiaries and they do not engage in taking management, operational or financial decisions affecting the group; and



- **they designate one of their subsidiaries established in the EU to fulfill the obligations** set out in CS3D on behalf of the ultimate parent company. The competent supervisory authority must grant the exemption. The ultimate parent company will remain jointly liable with the designated subsidiary for failure to comply with these obligations.

Scope and extent of due diligence

The material scope focuses mainly on corporate due diligence obligations. It covers human rights and adverse environmental impacts, defined by reference to the international conventions listed in the Annex to CS3D.

Due diligence is defined as an “obligation of means,” which requires companies to:

- **integrate** due diligence into their policies and risk management systems, and to draw up a specific due diligence policy including a code of conduct describing the implementation processes. This policy must be developed in prior consultation with the company’s employees and their representatives. It will be updated after any significant change and, in any case, every two years;
- **identify and assess** actual and potential adverse impacts on human rights and the environment arising from (i) their operations; (ii) those of their subsidiaries; and (iii) operations in their chains of activities;
- **prioritize** identified actual and potential adverse impacts based on their **severity and likelihood** when it is not possible to prevent, mitigate or bring to an end all identified adverse impacts at the same time;
- **prevent or mitigate** potential adverse impacts and **bring to an end** or minimize actual adverse impacts. Among others, by (i) developing and implementing prevention and corrective plans; (ii) seeking contractual assurances; (iii) making investments in production processes or infrastructure, and reviewing and improving their purchasing, design and distribution practices; and (iv) providing specific support to their business partners, especially SMEs.

Where it is not possible to prevent, mitigate, minimize or bring to an end an adverse impact in the chain of activities, companies may—as a last resort—temporarily suspend or terminate the business relationship;

- **remedy** actual adverse impacts and restore affected individuals or the environment to a situation equivalent to that which would have existed if the adverse impact had not occurred, including financial or non-financial compensation;
- **establish** and maintain a complaints procedure enabling potential victims, trade unions and civil organizations, among others, to file complaints when they have legitimate concerns regarding the actual or potential impacts of the companies’ own operations, those of their subsidiaries or their business partners in the chain of activities;



- **monitor** the effectiveness of the due diligence strategy and measures at least annually; and
- **publish** the due diligence process on their website. To avoid duplication, companies that prepare their sustainability report in accordance with the CSRD do not have to comply with this obligation.

Chain of activities

Due diligence in the chain of activities (replacing the previous term “value chain”) encompasses the following:

- **Upstream:** activities of **direct and indirect business partners** (including but not limited to design, extraction, manufacture, transport, storage and supply of goods or services).
- **Downstream** activities are limited to:
 - **direct business partners** (i.e., activities carried out for or on behalf of the company); and
 - **distribution, transport and storage** activities unless they are subject to export control by a Member State. **Waste management** activities are excluded.

Financial sector

- Regulated financial undertakings that meet the thresholds are subject to CS3D, with the exception of collective investment schemes and alternative investment funds under the [UCITS Directive](#) and the [AIFM Directive](#).
- Financial undertakings are **only subject to due diligence obligations for the upstream part of their chain of activities**. Therefore, downstream business partners receiving their services and products are excluded.

No later than two years after the entry into force of CS3D, the Commission must submit a report on the need for additional due diligence requirements for this sector.

Transition plan for climate change mitigation

- Companies subject to CS3D must adopt a transition plan to ensure, through best efforts, that their business strategy is **compatible with limiting global warming** to 1.5 °C, in line with the Paris Agreement. Also, if climate change is a major risk or impact of their operations, they must include emission reduction targets in their plans.
- The design of the transition plan must contain (i) time-bound targets related to climate change for 2030 and in five-year steps up to 2050; (ii) a description of decarbonization levers identified; (iii) an explanation and quantification of the investments and funding supporting



the implementation of the transition plan; and (iv) a description of the role of the administrative, management and supervisory bodies with regard to the transition plan.

- The plan must be updated annually, reporting on progress towards achieving the targets.
- CS3D eliminates previous versions' references to linking directors' variable remuneration to climate-related targets.

Supervision and penalty regime

One or more independent and expert national supervisory bodies will be set up to oversee the incorporation of CS3D into domestic law, as well as companies' compliance with the obligations deriving from it.

These bodies may impose sanctions on non-compliant companies, including:

- ordering cessation of infringements,
- adopting corrective measures,
- imposing financial penalties (depending on the company's turnover), and
- adopting interim measures to avoid irreparable harm.

Each Member State will establish its own sanctioning procedure, in line with its national legislation, including enforcement. These bodies may act on their own initiative and, in any case, will ensure that natural and legal persons have the right to submit "substantiated concerns" to any supervisory authority when they have objective reasons to believe that a company is in breach of its due diligence duties.

To reduce costs and improve supervision, coordination, investigation and information exchange, the Commission will establish a European Network of Supervisory Authorities.

Civil liability regime

Grounds for liability

- Companies will be held civilly liable for the damage caused to natural or legal persons where they:
 - (a) **intentionally or negligently fail** to prevent, mitigate or bring to an end potential adverse impacts on human rights and the environment under CS3D; and
 - (b) as a result of that failure, **damage is caused** to the **natural or legal person** protected by applicable law.



Legal standing

- In the case of **access to judicial remedies** for non-compliance resulting in damage, trade unions and civil or consumer organizations have **limited legal standing** based on the explicit consent of the alleged injured party.

Other issues

- CS3D recognizes the right of natural or legal persons to **full compensation** for the damage suffered, **excluding punitive damages**—i.e., deterrence through damages or any form of overcompensation (whether through penalties, multiple damages or other types of compensation).
- The **limitation period** for bringing actions for damages will be at least five years. Thus, the one-year limitation period for non-contractual (tort) liability actions under article 1968 of the Spanish Civil Code is extended.
- Companies **cannot be held liable if the damage was caused solely by their business partners** in their chain of activities.

The civil liability of a company is independent of that of its subsidiaries or business partners (if any). Where a company causes the damage jointly with its subsidiaries or (direct or indirect) business partners, they will be jointly and severally liable.

The use of third-party **verification** or contractual clauses to support the implementation of due diligence obligations does not automatically exonerate companies from liability.

- The civil liability regime provided for in CS3D is of **overriding mandatory application** where the law applicable to those claims is not the national law of a Member State.

EU support mechanisms

- CS3D includes **accompanying and support measures** for all companies, including SMEs, that may be indirectly affected by this new legislation. These measures comprise the creation of websites, specific information platforms or portals and tools, and potential financial support for SMEs.
- To support companies, the Commission may adopt guidance, for instance about voluntary model contract clauses. It will also issue guidelines on how to comply with the due diligence obligations set out in CS3D, including general guidelines and guidelines for specific sectors or specific adverse impacts. The Commission may also complement the support provided by Member States with further measures, including helping companies in third countries.



Implementation deadline

CS3D provides for a staggered implementation, with looser deadlines than those established in previous versions:

- **Three years (2027)** for the largest EU companies (5,000 employees and with a net worldwide turnover exceeding €1.5 billion) and non-EU companies meeting the above turnover threshold in the European market.
- **Four years (2028)** for EU companies with more than 3,000 employees and a net worldwide turnover of more than €900 million, and non-EU companies meeting the above turnover threshold in the European market.
- **Five years (2029)** for other companies.

For additional information, please contact our [Knowledge and Innovation Group](#) lawyers or your regular contact person at Cuatrecasas.

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