CSDDD- Corporate Sustainability Due Diligence Directive

In February 2022, the European Commission published a legislative proposal for a new Corporate Sustainability Due Diligence Directive (CSDDD). The CSDDD aims to reduce the risk of adverse human rights and environmental impacts arising within global value chains by setting out new requirements around how companies must conduct due diligence across their operations and value chains.

Under the proposed rules, companies will need to identify potential and real adverse human rights and environmental impacts connected to their own operations, subsidiaries, and business partners operating within their value chain. If real and/or potential impacts are identified, companies must take measures to prevent or mitigate potential impacts, as well as end or minimize real impacts. Due to the new rules' extraterritorial nature, coupled with ongoing supply chain disruptions, the compliance challenge is likely to be significant for companies within the scope of the CSDDD.

With time running out before the EU elections in 2024, EU lawmakers started to negotiate the final text of the CSDDD in the trilogue process at the beginning of summer. We anticipate that a formal deal could be agreed upon at the beginning of 2024 and, as a result, the CSDDD could enter into force in the first half of 2024. Member States would then have two years to transpose the Directive into national legislation, before then applying it to the largest companies as soon as 2027. Although 2027 may seem some way off, companies should start their implementation planning very soon – if they have not done so already – to ensure they have sufficient time and resources to comply with the requirements and navigate new and complex risks that will arise as a result of the Directive.

The Corporate Sustainability Due Diligence Directive (CSDDD) is a major piece of EU legislation that will require EU and non-EU companies to conduct environmental and human rights due diligence across their operations, subsidiaries, and value chains. Under the proposed rules, companies will need to identify potential and real adverse environmental and human rights impacts arising from their own operations, subsidiaries, and business relationships. Companies must take measures to prevent or mitigate any potential impacts they identify, as well as end or minimize any real impacts. If companies fail to comply and damage occurs as a result, they may be held liable and face financial penalties[1].

The CSDDD will also be the first piece of EU legislation that will mandate companies to adopt a climate transition plan. The requirements are expected to dovetail with the EU's CSRD and accompanying standards. EU lawmakers are currently negotiating the final text of the CSDDD in trilogues and are expected to reach an agreement in early 2024. Although everyone is waiting for clarification on certain areas of the Directive, companies can start to prepare their regulatory responses by taking some 'no regrets' actions to accelerate their preparations.

What should firms do?

The CSDDD may be subject to negotiations in a number of areas, but it is clear that the Commission, Council and Parliament all agree that corporate due diligence has an important role to play in sustainability. The Directive is unlikely to come into force until 2025 at the earliest, but given the political moves to make progress in this area, FS firms may find it helpful to pre-empt any mandatory actions and consider how some of their existing practices could be improved to align with the overall trajectory of the CSDDD[2]. Examples could include:

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1 https://www2.deloitte.com/uk/en/blog/emea-centre-for-regulatory-strategy/2023/what-is-the-european-corporate-sustainability-due-diligence-directive.html

2 https://kpmg.com/xx/en/home/insights/2023/02/the-eu-corporate-sustainability-due-diligence-directive.html

- Reviewing how director-level responsibilities are currently prescribed, and if there is any room for clarity in their governance maps when it comes to `sustainability' ownership; and
- Identifying any existing business practices that could be improved to demonstrate due diligence. General insurers in particular should take note and review their exposure management across multiple sectors, given their role in underwriting liability risks. Asset managers may wish to consider how their existing due diligence over investee companies could need to be enhanced.