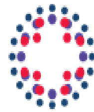

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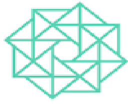

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Recommendations for the trilogue negotiations on the Corporate Sustainability Due Diligence Directive (CSDDD)

Introduction

The undersigned associations wish to contribute to the trilogue negotiations on the Corporate Sustainability Due Diligence Directive (CSDDD). We represent companies headquartered or with significant operations in non-EU jurisdictions, who are deeply committed to, and invested in the EU. We firmly support the goals of the Paris Agreement and the EU's objective to reach climate neutrality by 2050. Overall, we are supportive of the goals of the CSDDD proposal, as shown by the commitment of our Members to implement the UN Guiding Principles on Business and Human Rights (UNGPs) and the OECD Guidelines for Multinational Enterprises on Responsible Business Conduct.

In this context, we call on the EU co-legislators to ensure a workable and proportionate approach with a view to establishing a well-functioning framework. The EU has the unprecedented opportunity to provide guidance and global leadership, but to do that, it is of utmost importance that, while it develops its framework, it does not prevent other jurisdictions from doing the same. Global coordination and the establishment of global standards will be key to promoting respect for human rights and minimising adverse impacts on the environment in global value chains.

We also take note of the recent concerns expressed by French President Emmanuel Macron and Belgian Prime Minister Alexander De Croo with respect to the impact that the EU's ambitious sustainability regulatory agenda may have on the growth and competitiveness of the EU industry. In this context, we welcome the recent remarks by European Commission President Ursula von der Leyen announcing the objective of reducing reporting requirements by 25% to promote the competitiveness of EU businesses. We therefore urge the EU co-legislators to consider the impacts of the CSDDD on the competitiveness and attractiveness of the EU single market as well as the importance of making progress on financing the transition.

Extraterritorial impact of the CSDDD (Art. 2)

In the Commission's proposal and the Council's negotiating position, the CSDDD would apply to non-EU financial institutions active in the EU with a net EU turnover of more than EUR 150 million at the individual entity level (irrespective of whether they have a branch or a subsidiary in the EU), impacting the global business operations of non-EU financial institutions and the value chains originating from the entity in scope. The Parliament's position widens the extraterritorial application of the CSDDD, not only by lowering the EU turnover threshold to EUR 40 million but, most importantly, by extending the scope to the ultimate parent entity incorporated outside the EU.

The CSDDD is therefore expected to cover business activities that do not have any connection with the EU, which often represent the majority of the business activities of non-EU financial institutions, e.g. a loan from a non-EU bank to a non-EU business with activities exclusively outside the EU. On top of that, non-EU financial institutions would need to apply CSDDD due diligence to the entirety of their own and their subsidiaries' operations, covering all their suppliers, including those located outside the EU with no business nexus to the EU, e.g. an office canteen in a non-EU jurisdiction.

Specifically, requiring non-EU financial institutions operating globally to comply with the CSDDD requirements on value chains without any nexus to the EU will not only represent a disproportionate burden for non-EU financial institutions active in the EU, but it will also raise enforcement challenges and has the potential to conflict with similar third country obligations. Moreover, the competitiveness of both EU and non-EU financial institutions operating globally could be harmed as regional competitors outside the EU will not be subject to the same obligations. Clients and suppliers in jurisdictions outside the EU might be incentivised to favour local competitors that will not be subject to the CSDDD.

For these reasons, we believe that the **CSDDD's scope of application should be limited to the individual entity in scope, and the due diligence requirements should apply only to the value chain operations related to products sold in the EU and services provided in the EU.** This approach will not only ensure more proportionate obligations for non-EU financial institutions, but it will also improve the competitiveness of EU financial institutions operating globally and the overall attractiveness of the EU single market.

Definition of value chain for financial institutions (Art. 3g) and due diligence (Art.6 & 7)

In order to be able to fulfil the CSDDD due diligence obligations, financial institutions need to be provided with **clarity and legal certainty with regard to the definition of value chain and its boundaries. To address these issues, we recommend adopting a risk-based, proportionate approach for the application of the due diligence requirements.**

Accordingly, financial institutions' downstream value chain should be limited to the activities of large corporate clients directly receiving specific purpose loans and credits in the EU. This would prioritise the most critical and actionable risks, help mitigate the legal and implementation challenges faced by financial institutions, whose clients would already be captured directly by the CSDDD, and align to existing due diligence expectations for financial institutions. The provision of financing represents the area in which financial institutions have the most leverage with clients to achieve the objectives of the CSDDD.

The Parliament position requires financial institutions to identify actual and potential adverse impacts before providing a financial service (prior to client onboarding) and before subsequent financial operations. However, if all financial services fall under the scope of the CSDDD due diligence obligations as proposed by the Parliament, this requirement becomes impractical. Therefore, it is essential to emphasize that conducting due diligence before the provision of subsequent financial services will only be feasible if the value chain is limited to specific purpose loans and credits. We thus believe that the Council's general approach on the definition of in-scope financial services, to be relevant if Member States decide to make use of Article 2(8) to apply the Directive to financial institutions' business partners partners to which such financial institutions provide the specific services provided under Article 3(g), constitutes a possible starting point for the trilogue discussions on the value chain of financial institutions. In all cases, the scope of financial services covered should be defined in a targeted way, focusing on services which are capable of influencing sustainable impacts within the real economy such as lending.

Additionally, while the Parliament's position requires the continuous review of due diligence policies, the Commission's proposal and the Council's position recognise the importance of periodic reviews. We support the latter position as the requirement for continuous review of due diligence policies is unfeasible and would further burden financial institutions that will already face significant challenges to implement the CSDDD.

Definition of operations (Art.3)

According to the CSDDD proposal, the due diligence obligations apply to the operations of the entity in scope, to the operations of its subsidiaries, and to the business relationships of the entity in scope (Article 1 of the CSDDD). We understand that it is the intention of the legislator to distinguish between the operations of the company (entity in scope) and its subsidiaries, and the business relationships of the company (entity in scope). In the Commission's proposal and Council's position, the business relationships of the subsidiaries of the entity in scope are not subject to the CSDDD obligations (unless the subsidiaries meet the CSDDD application thresholds themselves). However, the Parliament potentially suggests the possible extension of the due diligence obligations to the upstream and downstream value chains of subsidiaries.

We favour the Commission and Council's approach and, therefore, suggest that the CSDDD provides a distinct definition of "operations", stating that **"operations" means operational activities of the company and its subsidiaries, and shall not include any business relationship.** Without a clear definition, there is a risk that during the transposition into national law, Member States could define "operations" in a way that also captures "business relationships". Different transpositions into national law would create an unlevel playing field in the EU, not to mention confusion for companies seeking to apply the rules and Member States seeking to supervise the application of the rules.

Definition of subsidiary (Art. 3)

The Parliament's negotiating position diverges from the Commission and the Council as regards the definition of "subsidiary". The Commission and Council define "subsidiary" as a legal person through which the activity of a "controlled undertaking" (as defined in Directive 2004/109/EC (Transparency Directive)) is exercised. On the other hand, the Parliament's position adds a reference to Directive 2013/34/EU (Accounting Directive) to define "subsidiary". In doing so, it potentially widens the definition to also include indirect subsidiaries by referring to "undertakings controlled by a parent undertaking, including any subsidiary undertaking of an ultimate parent undertaking". This change might have profound repercussions for fund managers given that funds, which are often "controlled" by their fund managers, as defined in the Transparency Directive, could be considered subsidiaries of a fund manager under the CSDDD.

As a result, if an in-scope fund manager exercises controlling influence over a fund, and that fund holds a majority stake in a portfolio company, it could be argued that the fund manager indirectly controls the portfolio company as well. In this case, the portfolio company might be considered a subsidiary of the fund manager under the CSDDD, potentially extending the due diligence obligations of the in-scope fund manager to the portfolio company. **We recommend the co-legislators maintain the definition of subsidiary proposed by the Commission which is only cross-referring to Directive 2004/109/EC (Transparency Directive) to define "controlled undertaking".**

Civil liability (Art. 22)

The Directive includes an obligation for companies to establish procedures that, inter alia, allow for complaints regarding actual and potential adverse impacts in relation to their business, their subsidiaries and their supply chains to be adequately addressed. The combination of the value chain

scope, due diligence requirement, and civil liability provisions presents legal risks for financial institutions attempting to comply with the proposed Directive.

The Directive allows a wide range of individuals to lodge complaints, which could potentially stimulate an influx of complaints due to the broadened legal standing. Furthermore, if companies are required to evaluate potential liability for the activities of businesses they finance, they may shy away from financing those firms for which the risk assessment or management is challenging, with the result that firms that e.g. need increased funding for their transition towards sustainability might not be financed. Another unintended consequence of these provisions could be undermining the competitiveness of financial institutions subject to these requirements, compared to larger regional banks operating outside of the EU that are not bound by the same rules.

To address those concerns, the civil liability regime under the CSDDD should be restricted to instances where a breach occurs intentionally or through gross negligence, leading to an adverse impact directly linked to the company's operations. Any civil liability should not be presumed in favour of the plaintiff.

Directors' duty of care (Art. 25 and 26)

The CSDDD also includes broadly worded changes to directors duties, bringing added liability and litigation risk. **We believe that an EU Directive should not seek to regulate directors' duties as Member States have different frameworks in place.**

Asset management (Art 8a)

The Parliament's position introduces an obligation for institutional investors and fund/asset managers (and possibly the funds which they control) to take appropriate and proportionate measures to induce their investee companies to bring actual adverse impacts caused by them to an end (Article 8a). This includes engaging with investee companies and exercising voting rights.

However, asset management's "investment value chain" is inherently different from traditional value chains as there is no direct contractual (legal) relationship between the investee company and the investor (institutional investors, asset managers acting on behalf of investors, etc.). Consequently, applying due diligence in the same manner as a contractual relationship is not feasible. While asset managers can (and usually do) engage with companies, the ultimate responsibility for business practices lies with the boards and management of the companies themselves, and it would not be possible for asset managers to ensure compliance of every investee company's responsibilities under the CSDDD. Furthermore, investee companies are not obligated to align with asset managers' recommendations, particularly considering that asset managers are often minority shareholders and cannot guarantee specific outcomes. It is also crucial to highlight the need to balance engagement with fiduciary duty and the investment mandates/objectives of the clients, which may or may not include ESG preferences. Article 8a fails to recognise these important elements specific to the activity of asset managers and disregards their role as fiduciaries.

Moreover, due diligence processes are already embedded within sectoral legislation, e.g. Sustainable Finance Disclosure Regulation (SFDR), the Directive relating to Undertakings for Collective Investment in Transferable Securities (UCITS), the Alternative Investment Fund Managers Directive (AIFMD), and Markets in Financial Instruments Directive (MiFID).

For these reasons, we strongly believe that **the investor-investee company relationship and investment management services should be excluded from the scope of the CSDDD. Consequently, Article 8a should be removed from the final text.**

Transition plans (Art. 15)

The CSDDD introduces mandatory transition plans for companies in scope, including for non-EU companies. We would like to highlight that non-EU financial institutions could be subject to obligations within their home jurisdictions to adopt transition plans aligned with the Paris Agreement. For example, in the UK there are already requirements for listed companies and large regulated asset owners and asset managers to disclose transition plans as part of their TCFD disclosures (on a comply-or-explain basis). Moreover, as set out in its 2023 Green Finance Strategy, the UK Government will shortly consult on requirements for the largest companies (including private companies) to disclose transition plans. Switzerland has introduced mandatory TCFD disclosures including on transition plans, and a number of jurisdictions globally have already signalled that they will adopt the IOSCO-endorsed ISSB climate disclosure standard, which includes transition plan disclosure.

Financial institutions operating globally develop their transition plans to reach global net zero at group level, rather than individual regional entity level. However, given the different transition pathways of each jurisdiction, transition plans developed according to the EU rules might not be compatible with those developed at group level according to third country rules. Overlapping and conflicting requirements will make it more difficult for non-EU financial institutions to develop a coherent and consistent plan to align their overall business model and operations with a net zero economy, undermining the overall decarbonisation effort. Most importantly, applying EU-based transition plan requirements to financial institutions' global operations could inadvertently create challenges for global decarbonisation efforts, both through impacts on developing countries and impacts on clean energy supply chain financing and investment.

We therefore invite the co-legislators to ensure that requirements laid out in the **CSDDD will not exceed the specifications of transition plans included in the European Sustainability Reporting Standard (ESRS) E1-1, and that the requirement to have a transition plan will be fulfilled by compliance with ESRS E1-1.** Prescriptive specifications of the characteristics of transition plans risk constraining financial institutions' global business strategy and ability to support the transition in jurisdictions outside the EU.

Lastly, linking the variable remuneration of directors to the achievement of the very long-term objective of transition plans does not take into consideration the fact that directors' variable remuneration are determined each year for a performance period limited to 12 months. Moreover, as climate objectives are not defined to date with a yearly measure of progress, it is difficult to see how this requirement could be implemented. We would also note that the disclosure requirements under the CSRD/ESRS which prescribe the disclosure of information about the integration of the sustainability-related performance in incentive schemes (ESRS 2 - GOV-3) do not refer to companies' transition plans. Finally, we would like to remind the co-legislators that the ability of shareholders to influence a company's remuneration policy is already fully addressed by the Shareholder Rights Directive (SRD) (Directive 2017/828) which also requires that the remuneration policy must include the company's long-term interests and sustainability. We therefore consider the inclusion of the issue of remuneration in this Directive unnecessary and would support the Council's position to remove this provision (Article 15(3)).