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EU Mandatory Human Rights Due Diligence Legislation to Be Proposed in Early 2021

At the end of April, EU Commissioner for Justice Didier Reynders announced that the European Commission will introduce mandatory human rights due diligence legislation in the first quarter of 2021. The legislation will be part of the EU's COVID-19 recovery package and the European Green Deal.

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Many of the details of the legislation to be proposed remain to be determined. However, it is a certainty that, if adopted, EU human rights due diligence legislation will have a significant impact on U.S.-based companies, either directly by virtue of their EU operations or indirectly due to their place in the supply chains of companies subject to the legislation.

In this Alert, we discuss the likely contours of the legislation that will be proposed and other related developments in the rapidly evolving area of mandatory corporate human rights due diligence.

European Commission Study on Due Diligence Requirements Through the Supply Chain

Commissioner Reynders' announcement was made in conjunction with a webinar hosted by the EU Parliament's Responsible Business Conduct Working Group to discuss a study on due diligence through the supply chain commissioned by the European Commission's Directorate-General for Justice and Consumers. The mandate for the study derived from the Commission's March 2018 Action Plan on Financing Sustainable Growth and the Parliament's May 2018 Report on Sustainable Finance.

The study was undertaken by the British Institute of International and Comparative Law in partnership with Civic Consulting and LSE Consulting. The final report, which was published in February and clocks in at almost 600 pages, is intended as an initial study for the possible development of human rights due diligence regulatory options at the EU level.

The study examined current market practices and the regulatory framework applicable to due diligence for human rights and environmental impacts in the European Union and selected non-EU jurisdictions. In addition, as part of the study, the pros and cons of several regulatory options were examined, as further discussed below.

In connection with the assessment of current market practices, surveys and interviews were conducted with business survey respondents (334) and general survey respondents (297). The latter category included business associations and industry organizations, civil society, worker representatives and trade unions, legal practitioners and government bodies.

Regulatory approaches examined were broken down into four broad options: (1) no policy change; (2) new voluntary guidelines or guidance; (3) new regulation requiring due diligence reporting (analogous to current disclosure-only modern slavery legislation); and (4) new regulation requiring mandatory due diligence as a legal duty of care. The last option was further broken down into sub-options that considered sector coverage, company size, remedies and oversight and enforcement.

Selected significant observations and conclusions from the study include the following:

- Just over one-third of business respondents to the survey indicated that their companies undertake due diligence that takes into account all human rights and environmental impacts, with another third undertaking due diligence limited to certain areas.
- A majority of business respondents undertaking due diligence include first tier suppliers only.
- Human rights and climate change processes often take place in silos.
- Survey respondents (both business and general respondents) indicated that the current legal landscape (option 1) does not provide companies with legal certainty about their human rights and environmental due diligence obligations, and it is not perceived as efficient, coherent and effective.
- Interviewees agreed that there is already enough voluntary guidance (option 2). Overall, respondents seemed unconvinced that new voluntary guidance would have notable social, environmental and human rights impacts.
- Survey respondents were more positive about the likely sustainability impacts of new regulatory reporting requirements. However, perceived shortcomings of this approach were noted, in particular, that reporting requirements do not usually provide for effective sanctions for non-compliance and do not substantively require appropriate due diligence for compliance with the regulatory obligation. It was nevertheless highlighted that reporting requirements have had a positive impact. It also was noted that some are relatively new, which has likely not given them sufficient time to achieve their full impact.
- The majority of stakeholders indicated that mandatory due diligence as a legal standard of care (option 4) may provide potential benefits to businesses due to harmonization, legal certainty, a level playing field and increasing leverage in their business relationships throughout the supply chain through a non-negotiable standard. Almost all interviewees were in principle in favor of a policy change to introduce a general standard at the EU level, although they differed on aspects of liability and methods of enforcement.
- Within option 4 (mandatory due diligence), there was an overall preference for a general cross-sectoral regulation that takes into account the specifics of particular sectors. Survey respondents expressed an overall preference for a standard that applies irrespective of size, but, not surprisingly, views varied on this point.
- Stakeholders indicated that the legal mechanism should be based on a standard of care, rather than a procedural, check-the-box requirement. In addition, stakeholders indicated that companies should be able to avoid legal liability by exercising appropriate due diligence.
- Stakeholders suggested that any regulatory mechanism should build upon the influence and strength of the due diligence concept contained in the UN Guiding Principles on Business and Human Rights.
- Company and industry association survey respondents appear to be somewhat out of sync. Many companies indicated support for a mandatory due diligence regulation, while the majority of industry organization respondents appear to be in favor of the least enforceable regulatory options.
- Social impacts from option 4 (mandatory due diligence) are expected to be the most significant, although the magnitude and nature of the impacts would depend upon the design and application of the regulation, the social issues addressed and the effectiveness of enforcement mechanisms. Options 2 (new voluntary guidance) and 3 (new reporting requirements) are expected to have only minor positive social impacts, because they do not require companies to take any new due diligence measures and are therefore viewed as unlikely to result in companies doing so.

The study's observations and conclusions will undoubtedly inform the debate over the legislative proposal and its ultimate content, and some of the foregoing items from the study were noted by Commissioner Reynders in his remarks during the Parliamentary working group webinar.

Fleshing Out the Legislative Proposal

Although significant details remain to be determined and further fleshed out, Commissioner Reynders noted his views on selected aspects of the proposed legislation during the webinar, in response to questions raised by members of Parliament and other webinar speakers:

- Due diligence should be mandatory.
- The legislation should be cross-sectoral, possibly with additional sector-specific elements.
- There should be an enforcement mechanism and sanctions for non-compliance.

DG for Justice and Consumers will be launching a public consultation on sustainable corporate governance and due diligence, which also will inform the Commission's legislative proposal.

Looking Ahead

Existing laws that require corporate human rights due diligence – such as the French Duty of Vigilance Law, the U.S. Conflict Minerals Rule, the EU Conflict Minerals Regulation and the U.S. Federal Acquisition Regulation anti-trafficking provisions – apply to a relatively small number of companies and/or a narrow set of issues. In the coming years, we expect human rights due diligence across a broader range of issues to be mandatory for a substantially larger number of multinationals, including those based in the United States.

Corporate human rights due diligence legislation with broader impact is awaiting adoption, has been proposed, has been called for by civil society stakeholders and/or is at the discussion stage in several jurisdictions, including Belgium, Canada, Denmark, Finland, Germany, the Netherlands, Norway, Switzerland, the United Kingdom and the United States. Recent developments in the Netherlands, Norway and the United Kingdom are discussed in our earlier alerts [here](#), [here](#) and [here](#), respectively. In addition, at the United Nations, negotiations to develop a binding human rights treaty have been ongoing since 2015.

Given the momentum behind mandatory human rights due diligence at the EU level, EU legislation is likely. In addition to support at the Commission, there is support in the Parliament and the Council. In its April 17 resolution on EU coordinated action to combat the COVID-19 pandemic and its consequences, the Parliament indicated that, as part of a stronger post-crisis Union that delivers more effective action to its citizens, it is convinced that corporate human rights and environmental due diligence are necessary conditions in order to prevent and mitigate future crises and ensure sustainable value chains. In addition, on April 29, Bernd Lange, the Chair of the Parliament's Committee on International Trade, published a position paper in which he advocated for a binding supply chain law. According to the position paper, the law should obligate companies to carefully examine their human rights and environmental risks and their susceptibility to crises and to take appropriate measures to prevent and mitigate such risks. It also appears that legislation will have the support of Germany when it assumes the Presidency of the EU Council for the second half of 2020.

As indicated by the limited survey conducted in connection with the Commission's due diligence study, there also is support within the business community for mandatory human rights due diligence, including at leading multinationals. Separate from the survey, individual companies and groups of companies in various EU countries, including Germany and the Netherlands, have come out in favor of mandatory human rights due diligence. However, not surprisingly, support within the business community is mixed, since businesses ultimately will be the ones required to shoulder the costs of compliance and bear the risks of liability.

As part of the continuing integration of ESG factors into investment decisions, investors also are calling for mandatory human rights due diligence. In the lead-up to the Parliamentary webinar, on April 21, the Investor Alliance for Human

Rights, an initiative of the Interfaith Center on Corporate Responsibility, released a statement calling on all governments to develop, implement and enforce mandatory human rights due diligence requirements for companies headquartered or operating within their own jurisdictions or, where appropriate, to strengthen regulatory regimes that already exist. Among other things, the Investor Alliance for Human Rights statement notes that proper and comprehensive human rights due diligence by companies, including mandatory and meaningful disclosure, enables investors to identify the greatest risks to people in investors' portfolios and make informed and responsible investment decisions. To date, more than 100 investors representing approximately \$5 trillion in assets under management have signed on to the statement, including some mainstream investors with significant assets under management.

Up until the adoption of EU corporate human rights due diligence legislation (and likely even thereafter), we expect the debate to continue to be robust due to differing views among legislators and other government branches, civil society and the business community over, among other things, the conduct to be covered, the entities to be subject to the legislation, the extent of the due diligence obligation, liability and enforcement mechanisms. The current economic environment will place additional pressure on legislators to strike an appropriate balance between human rights and economic considerations, which is likely to further intensify debate.

Even though legislation is expected to be proposed in early 2021, an EU-wide corporate human rights due diligence obligation is likely at least several years away. In the more limited context of conflict minerals due diligence, an EU regulation was adopted in 2017 (seven years after U.S. conflict minerals legislation). That regulation does not take effect until the beginning of 2021. Underscoring the difficulty of reaching a broadly acceptable approach to mandatory human rights due diligence, legislation in the Netherlands and Switzerland, which are further along in the process, has been several years in the making.

Even in the absence of additional legal requirements, many U.S.-based companies have been expanding their human rights due diligence compliance programs over the last few years. We expect the incremental evolution of these programs to continue. There are many drivers contributing to this trend. Greater awareness is one factor. Although the Commission-sponsored study noted shortcomings in the effectiveness of disclosure-only corporate human rights requirements, corporate modern slavery legislation has increased awareness of human rights issues in supply chains. Consumer and commercial customer considerations also have been factors. In addition, the continuing shift toward stakeholder capitalism, as articulated in the Business Roundtable Statement on the Purpose of a Corporation and the Davos Manifesto, has been a factor. Investor considerations and pressures also have resulted in change. Many public companies are bolstering human rights compliance programs in response to the increasing number of human rights-related shareholder proposals over the last few years, as well as in response to human rights compliance indicators measured by ESG data analytics providers. Finally, evolving supply chains and supply chain pressures brought about by the COVID-19 pandemic, tariffs and other issues are becoming bigger human rights compliance program drivers.

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