Regulating the Sustainability Transition

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The European Parliament's adoption of its position on the Corporate Sustainability Due Diligence Directive (CSDDD) last week marks a breakthrough for transnational corporate regulation. At a moment when the EU Green Deal was facing open opposition from within the European People's Party Group (EPP), rapporteur Lara Wolters (S&P) withstood lobbying efforts until the final minute and secured a majority for her report. With a strong mandate for the Parliament in the upcoming Trilogue, the EU has come a big step closer to passing the most ambitious due diligence legislation worldwide.

The EU legislation will be the apex, for now, of the transnational movement around corporate accountability for human rights violations. Ten years ago, the factory collapse of Rana Plaza in Bangladesh epitomized the weak regulatory framework for global value chains where, in law and broader parts of public opinion, rights violations along value chains were considered 'too remote' to be connected to the responsibilities of lead firms. Since then, much has changed in political discourse, consumer perception and ultimately also legal baselines. The catalyst has been a unique set of transnational rules, the UN Guiding Principles on Business and Human Rights (UNGP) of 2011. The UNGPs redefined the terms of the debate around corporate accountability with respective responsibilities of states, companies and civil society and put forward 'due diligence' as a new legal mechanic through which lead firms ought to scrutinize their value chains. Like the German Supply Chain Act of 2021, the CSDDD largely follows the UNGP, it is transnational both in its reach and the origins of its underlying concepts.

Mandatory due diligence between rights and risks

The UNGP sought to infuse human rights into business operations and used 'due diligence', a concept that seemed familiar in the world of business, to translate human rights into the private sphere. This move driven by 'principled pragmatism' was characteristic of the mind behind the UNGP, international relations scholar and diplomat John Ruggie. In terms of legal conceptualizations, his key achievement was two-fold. First, the UNGP sideline lengthy debates on the 'horizontal' applicability of human rights that had created a deadlock in national and international debates. The procedural nature of due diligence turns human rights into performance benchmarks and shifts the debate from the level of interpreting rights to the mechanisms of controlling compliance. Second, the UNGP extend the sphere of responsibility beyond contracting parties and give meaning to the many mediated relationships and interconnections that mark the global economy.

Tracing such dynamics between the global and the local, between lead firm practices and working conditions at small suppliers, between economic interests, environmental footprint, and development requires adopting a *systems perspective* that breaks some of the cognitive and legal frames that work to dissociate and invisibilize, rather than integrate such dynamics. In particular, the UNGPs contest the boundaries that the concepts of contract and corporate personality draw for individual responsibility. The conceptual innovations come at the price of exposing human rights to a logic of risk assessment in which companies enjoy broad interpretive and managerial authority. The UNGPs reshuffle our understanding of public and private means of regulation in a potentially very impactful, yet also fragile manner that is prone to corporate capture. It is important to note this inherent tension in the idea of effective protection of rights through a procedural framework of corporate risk assessment, which is at the bottom of many debates around the CSDDD.

The European Parliament's position

Within the EU, the Parliament has been a critical actor for the CSDDD from the start after calling for corporate due diligence in a 2021 resolution. The Parliament's position adopted last week goes beyond the EU Commission's initial proposal and the EU Council's position in several important respects. The amount of amendments testifies to the fact that value chain due diligence is a new mode of regulation that raises a host of open questions for legislative design. The Parliament agreed to expand the notion of 'value chain' to include not only suppliers of goods and services, but also downstream activities such as sale, distribution, and transport (while excluding consumption). It further expressed support for a lower threshold for the personal scope of application both for EU-based and non-EU companies and wants to see the financial sector included. Moreover, MEPs strengthened the mix of enforcement mechanisms, not only by expanding provisions on civil liability but also around administrative oversight and sanctions. The latter may go up to 5 % of the net worldwide turnover and include suspension from public procurement. Lastly, the Parliament substantiated the environmental and climate side of due diligence which is still gaining contours in international documents and practice. Due diligence shall also relate to the Paris Agreement and companies are expected to formulate a 'transition plan' tied to directors' remunerations that can be a powerful decarbonizing instrument alongside due diligence.

Attaining root causes of unsustainable corporate conduct

How effective can such a refined due diligence legislation be? Some have pointed to the need for a clear inclusion of workers' voice and the problematic role played by social audits and certification – despite their many well-established shortcomings. Mandatory due diligence indeed does not overcome previous regulatory paradigms of private governance and transparency, but makes them a building block of due diligence. However, the Parliament's position takes a big step ahead by

acknowledging how rights violations are often intrinsic to business models. Establishing this connection requires seeing rights violations as in-built features of value chain organization rather than as sporadic cases of wrongful individual management decisions. For example, through excessively short order timelines as known under the 'fast fashion' model and by price squeeze along the chain, lead firms contribute to highly volatile supplier relations and vulnerable working conditions on the ground. While a bit under the radar of the public debate, the Parliament's position introduces references to living wages and business models that open the door to a more structural critique of corporate practices in today's economy.

On the other side, the Parliament backs or introduces several practical tools of standardizing compliance that might further a culture of routinised checkbox due diligence. Those include the development of guidance on due diligence by the Commission, the formulation of model contract clauses to be used towards suppliers and the endorsement of value chain management IT to operationalize due diligence. In addition, there will be particular assistance for small and medium enterprises (SMEs). Those tools are a reaction to business demand for more 'legal certainty' – a claim that had already been made prominent by the EU's Regulatory Scrutiny Board in its back-to-back negative opinions on the impact assessment by the Commission. Legal certainty, however, has a different bearing in due diligence legislation than under previous command-and-control forms of regulation. The openness of the due diligence procedure stems from its aspirational, reflexive and participatory character. It invites companies to develop tailored mechanisms and priorities within broad margins – rather than subjecting them to unpredictable state sanctioning, as in the liberal understanding of legal certainty as a bedrock of the rule of law. The French Constitutional Court had missed this point in its 2017 decision invalidating parts of the French due diligence law. Going forward, this changing role of legal certainty needs to be exposed. Arguments of legal certainty here often work in favor of a minimalist, standardized and unambitious due diligence process.

What to expect in the Trilogue: Push for full harmonization?

Next to questions of scope and civil liability, the degree of European harmonization will be a central issue in the starting Trilogue negotiations. As a Directive, the CSDDD does not automatically require full harmonization but allows Member States to have stricter rules consistent with the Directive's goals. But the creation of a level-playing field overcoming national fragmentation was a central aspiration of the EU Commission and was highlighted in the Parliamentary resolution of 2021. Companies have also lobbied for a uniform legal framework. The Parliament refrained from framing the CSDDD as full harmonization, but included a 'Single Market Clause' that requires 'coordination' towards full harmonization and foresees an evaluation after six years to consider a conversion of the Directive into a Regulation. Maintaining Member States' ability to expand the scope and enforcement mechanisms will be important. Due diligence remains an emerging regulatory mode for which input and innovation from different regulators are welcome – similar to the early days of EU consumer law before the acquis consolidated.

At the very least, if the EU and the Commission narrow the space for Member States' initiatives, they will bear a heavy responsibility of updating and adjusting due diligence in exchange with stakeholder groups. Furthermore, the timing of the release of the updated OECD Guidelines for Multinational Enterprises earlier this week underlines that standards and interpretation of due diligence will be subject to transnational regulatory competition.

The EU Green Deal and the mode of law for the sustainability transition

The CSDDD is a cornerstone of the EU Green Deal and as such complemented by several other legislations and agendas, including the Deforestation Regulation, the Conflict Minerals Regulation, the proposed Forced Labour Regulation and the overarching EU Circular Economy Action Plan. In times of trade disruptions and scarce critical commodities, sustainability becomes intertwined with geopolitics, as regulators around the globe growingly use global value chains as a regulatory proxy to attain different policy objectives, including the security of supply. Due diligence has been criticized as protectionist, placing excessive burdens on small suppliers in the Global South and failing to generate a positive impact on development.

The CSDDD has yet to find its place in a contested transnational regulatory space while remaining sensitive to the local differences it encounters across its diverse contexts of implementation along global value chains. The entangled transitions of systems of production, food, mobility, construction, energy and more will require a mode of law that reflects systemic dynamics and integrated thinking about different ecologies of law—a generational project which Horatia Muir Watt calls 'law's ultimate frontier'. Due diligence can be part of such an emerging mode of law. The current shape of due diligence will not bring this search for a new legal consciousness to an end. Rather, as John Ruggie argued for the UNGP, 'it marks the end of the beginning.'