International Federation of the
Economy for the Common Good e.V.

Internationaler Verband der Gemeinwohl-Ökonomie
Stresemannstr. 23
22769 Hamburg, Germany
Transparency Register: 339093641078-19
https://www.ecogood.org/
https://www.ecogood.org/apply-ecg/common-good-matrix/

For further information, please contact
the ECG EU Advocacy Team:
Walter Kern walter.kern@ecogood.org
+49 6222 660241 / +49 176 47643355

Position paper on the Corporate Sustainability Due Diligence Directive

August 2022

The Economy for the Common Good (ECG) is a social movement advocating for a future-fit economic model which is beneficial to all stakeholders of an organisation: employees, suppliers, customers, business partners, the local community and society at large, as well as the planet and future generations. It is a model that declares the common good, i.e., the well-being of people and respect for all life, as its supreme goal and purpose, building on four ethical pillars: Human Dignity, Solidarity and Social Justice, Environmental Sustainability, Transparency and Participation.

The ECG movement is constantly growing and gaining supporters across EU Member States. So far, more than 1.000 organisations, mainly companies, but also schools, universities, municipalities and cities, have used our Common Good Balance sheet as a means to change their business practices and conduct their "non-financial" reporting, including to meet their obligations under the current Non-financial Reporting Directive.

In this position paper we explain why EU decision-makers should consider the Common Good framework to build a more robust and ambitious **Corporate Sustainability Due Diligence Directive** (CSDDD).

In our view, the Commission proposal is a good basis, but must be strengthened by the Parliament and the Member States to make a significant contribution to better sustainability due diligence:

1. Sustainability due diligence should cover **the whole value chain** (upstream and downstream), in a risk-based and proportionate manner.
2. Sustainability due diligence should cover **all human rights and environmental impacts** (including climate) as provided for in the international agreements to which the directive proposal refers.
3. Sustainability due diligence (and reporting) should be extended to **all companies** which fall under the obligation of financial reporting.
4. Sustainability due diligence should **consider the perspective of those affected** based on their affectedness and meaningful consultation of stakeholders in all phases of due diligence processes.
5. Company boards should be required to **integrate sustainability risks and impacts into their corporate strategy, risk management, control and compliance systems.**
6. **Variable remuneration** for board members should be **linked to the company's sustainability performance.**
7. The **burden of proof must be on the company** to demonstrate whether it acted reasonably or not.

Recommendations on the Corporate Sustainability Due Diligence Directive

ECG highly welcomes the fact that an EU-wide harmonized regulation of value chains is underway. This is a positive initiative that has the potential to ensure companies cannot benefit from the economic opportunities offered by global markets and value chains without respecting a set of fundamental human rights and environmental standards. If the right level of ambition is reached, this directive has the potential to rebalance today's asymmetric regulatory landscape and to create a level-playing field where the activity of global companies is structured around a new paradigm of both rights and obligations.

This initiative is all the more welcome given several international attempts to introduce legal corporate obligations recently failed due to massive lobbying by UN member state governments, e.g. the "Norms on the Responsibilities of Transnational Corporations and Other Business Enterprises with Regard to Human Rights"[1] in 2004. A "binding treaty" is currently being negotiated[2], but progress is slow and engagement from wealthier country governments is weak.

1. A holistic and consistent approach towards CSRD, CSDDD and SFDR should be favored

Two EU legislations related to corporate sustainability are being developed in a short timeframe: one on reporting requirements (CSRD), the other on due diligence (CSDDD). In that context, ECG would like to point at the inconsistencies that might be created by the parallel development of (i) reporting standards in the European Financial Advisory Board (EFRAG) and (ii) due diligence obligations, including for board members. One could extend this analysis of increasing piecemeal regulation to the financial sector as well, as the Sustainable Finance Disclosure Regulation (SFDR) developed a third set of criteria for financial market actors. Same holds true for the EU Directive on public Country-by-Country reporting (CbCR) which should be considered at least in the European Sustainability Reporting Standards (ESRS).

ECG therefore supports to reinforce consistency through the development of a holistic set of sustainability standards relevant to all three areas: a) reporting requirements, b) due diligence requirements and c) financial market requirements, valuations, and ratings.

2. The proposal should be strengthened by implementing the suggestions laid out below

Together with other civil society organizations (CSOs), ECG has developed a set of concrete recommendations to EU co-legislators to strengthen the Commission's proposal and to close the gaps created by the shortcomings collectively identified. ECG was notably involved in the drafting of a CSO public letter[3], and co-signed[4] another. Most important suggestions for improvement include:

- **Ensure due diligence obligations are not restricted to "established business relationships".**
  Restricting due diligence to "established business relationships" does not create the necessary conditions for an effective and robust duty to prevent and end harmful human rights and environmental impacts throughout the whole value chain in a risk-based and proportionate manner. It could allow companies to restructure their value chains to avoid implementing due diligence obligations.
- **Enlarge obligations to additional human rights and environmental impacts.**
  The definitions of adverse human rights and environmental impacts must be comprehensive and expanded to cover all human rights and environmental impacts (including climate) as also provided

1 https://digitallibrary.un.org/record/498842
2 https://bindingtreaty.org/
3 https://www.ecogood.org/ecg-co-signed-a-ngo-recommendation-on-csddd/
4 https://www.ecogood.org/ecg-and-over-220-civil-society-groups-call-for-eu-corporate-sustainability-due-diligence-law-to-be-strengthened/

for in the international agreements to which the CSDDD refers, i.e. the UNGPs and the Paris Climate Agreement.

- **Expand the scope of the proposal beyond companies with more than 500 employees and those with more than 250 employees from selected risk sectors.**
  What is needed is the inclusion of all companies, including small and medium-sized enterprises (SMEs), in the scope of the proposed directive, with a risk-based approach. Impacts on people and the environment do not depend exclusively on the size of a company, but rather on the industry in which a company operates, its business model and the ethical attitude of its management. Moreover, more than 99% of the European economy is made up of SMEs, which means that the scope of the CSDDD proposal covers less than 1% of all companies. Consequently, the scope of the directive should be extended to all companies which fall under the obligation of financial reporting.
- **Reinforce stakeholder consultation in due diligence.**
  The CSDDD should ensure that the perspective of those affected is fully considered, based on affectedness and through the meaningful consultation of stakeholders in all phases of due diligence processes, e.g. through the establishment of Stakeholder Advisory Councils/Boards. In addition, the protection of people and communities, as well as human rights defenders and environmentalists, from retaliation and adverse consequences should be strengthened. The rights of indigenous people to self-determination and to free, prior, and informed consent should also be explicitly included in the directive.
- **Company directors' obligations should be clarified.**
  Corporate boards should be obliged to integrate sustainability risks and impacts into their corporate strategy, target system, and controlling. Proper guidance on this could be taken from the new German Corporate Governance Code (DCGK) 2022[5].
- **Variable remuneration linked to corporate sustainability performance.**
  The variable remuneration of board members should be directly linked to corporate sustainability performance, at least to the same extent as to financial targets.
- **Provisions on civil liability and access to justice should be strengthened.**
  The burden of proof must lie with the company to demonstrate whether or not it has acted reasonably. This burden must not be placed on the plaintiff, who has limited resources and little access to evidence. Companies must also be liable for if they have attempted to achieve compliance through contractual means and audit/verification processes. In addition, independent non-profit organizations that have a legitimate interest in representing victims must also be given the right to act on their behalf.

In addition to the aforementioned recommendations, ECG calls on policymakers to elevate the level of ambition of the proposal through the integration of two additional suggestions: one on to strengthen global governance (A) and the other to promote responsible purchasing practices (B).

(A) To reinforce global governance, ECG calls on the establishment of a long-awaited World Court of Human Rights

The establishment of such a court would help bridging the gap between codified human rights and reality. As proposed by Nowak, Scheinin and Koza[6], with a World Court of Human Rights – legally based on a list of twenty-one international agreements for the protection of human rights –, the duty to uphold human rights would apply to both countries and business agents. In an initial phase, corporations could voluntarily recognize the competence of the court. At a later stage, companies might be held accountable if their headquarter is located in a country recognizing the competence of the Court. By advocating for the

5 German Corporate Governance Code (as amended on 28 April 2022): https://dcgk.de//files/dcgk/usercontent/en/download/code/220627_German_Corporate_Governance_Code_2022.pdf

6 Julia Kozma, Manfred Nowak, Martin Scheinin (2011): A World Court of Human Rights – Consolidated Statute and Commentary.

establishment of such a court, the EU would ensure that the protection of human rights take precedence over investors' rights.

(B) ECG suggests requiring responsible purchasing practices from market participants

Responsible purchasing practices are an important prerequisite for respecting human rights and protecting the environment by companies and their supply chains. The common framework[7] published this year by a group of different multi-stakeholder initiatives, which is based on the recommendations[8] of the Sustainable Terms of Trade Initiative, could serve as a basis for implementation. It defines responsible purchasing practices as well as the conditions for an effective partnership between purchasing companies and suppliers by improving working conditions in supply chains, paying living wages and building resilience in the supply chain. This, and more, is already inherent to the value-based framework proposed by ECG, which could be transposed into European law.

3. The CSDDD could help redefine the social role of companies

ECG supports that the end of businesses cannot be to only generate profit. Instead of primarily seeking financial gain, companies should have a meaningful purpose. Participating to the creation of a form of common good should be the overriding goal of all business activities.

This is supported by several constitutional texts. The Bavarian Constitution for example states in its article 151 that "economic activity in its entirety serves the common good." As clearly presented by Sjåfjell and Mähönen[9], this means for companies to evolve from being collectors of power relationships between shareholders and stakeholders to be meaningful enablers driven by a socially and environmentally sound purpose. Velte and Weber[10] stress the need for a sustainable corporate purpose as “long-term value creation for firms *and* society in line with the UN SDGs to recognize the two perspectives of sustainability (time-driven as long-term and content-based as UN SDGs)“.

Democratic core values and their protection and fulfillment should constitute the basis of a company's strategy, business development, due diligence and reporting activities. Board members should be liable for ensuring that these values are not violated, and financial market actors should be able to assess how any form of financing can affect a company’s ethical baseline. Using a comprehensive and democratically defined “common good” as a baseline would ensure that financial resources such as capital or return on investment are only means to an end, and not the overarching purpose of economic activity.

7 https://www.textilbuendnis.com/en/purchasing-practices-framework/

8 Sustainable Terms of Trade Initiative (2021): White Paper on the Definition and Application of Commercial Compliance.

9 Beate Sjåfjell, Jukka Mähönen (2022): Corporate Purpose and the Misleading Shareholder vs Stakeholder Dichotomy

10 Patrick Velte, Stefan, Weber (2021): Sustainable corporate purpose and sustainable corporate governance: Integrative theoretical framework and reform recommendations, Journal of Environmental Law and Policy 3/2021, p. 287-323.