Briefing note on the EU Corporate Sustainability Due Diligence Directive (CSDDD) and implications for sustainability systems
Considerations of industry schemes, multi-stakeholder initiatives and third-party verifications in the latest draft of the regulation

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This briefing paper complements ISEAL’s Recommendations, released in November 2022, which focus on two main areas of legislative reform for the EU Corporate Sustainability Due Diligence Directive (CSDDD):
- Strengthening the role of industry schemes, multi-stakeholder initiatives and independent third-party verification as tools for due diligence compliance;
- Amplifying the role of such industry schemes, multi-stakeholder initiatives, and independent third-party verification in delivering collaborative and impactful due diligence that goes beyond what is legally required from companies.

This briefing paper further unpacks the implications of the CSDDD for industry schemes, multi-stakeholder initiatives and independent third-party verification. The analysis is based on the current state of affairs on the CSDDD, following the respective positions of the European Commission (February 2022), the Council (December 2022) and the European Parliament (June 2023). These three institutions are currently negotiating the ultimate legislative text in the final stage of the legislative process, the so-called ‘Trilogue’.

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1. The EU CSDDD: state of the legislation

The European Commission’s proposal of February 2022 sets out a comprehensive framework for due diligence along supply chains. It requires large companies incorporated or operating in the EU to ‘identify, prevent and mitigate’ any adverse impacts on human rights and the environment along their supply chain. While the European Council in its position generally favoured a less imposing formulation, the European Parliament’s position seeks to make the Directive more effective by expanding the scope of companies covered as well as the nature of due diligence obligations and their enforcement.

At this stage, several central aspects remain under debate and will only be spelt out in the ongoing negotiations between the Commission, the Parliament and the Council (‘Trilogue’). The Directive will likely be formally adopted in late 2023/early 2024 and EU Member States will then have two years to transpose the CSDDD into national legislation. In-scope companies will need to become compliant over the next years, likely according to a gradual phase-in that obliges the biggest companies first and leaves more time for less big companies.1

As it stands, the CSDDD explicitly mentions and defines ‘industry schemes or multi-stakeholder initiatives’ and ‘independent third-party verification’ as tools that can assist companies in achieving compliance. The proposed Directive acknowledges their positive contribution. Both terms do not necessarily encompass the totality of schemes and initiatives on sustainability covered by the ISEAL Codes. Terminology and definitions on this point might still be shifting in the legislative process. More details are provided in “4. The roles of ‘industry schemes or multi-stakeholder initiatives’ as well as ‘third-party verification’”.

2. Scope and relation to other due diligence regulations

The proposed Directive aims to create a level playing field in the realm of sustainability due diligence. It is a direct response to the multiplicity of national and international rules and private initiatives that exist in this area. For many companies, the requirements of the CSDDD will be similar to existing voluntary sustainability practices, including those required by verification schemes and industry initiatives. However, the CSDDD profoundly alters their context, turning voluntary, ethical and/or market-induced efforts into legally prescribed obligations.

The CSDDD is expected to emerge as the dominant framework for corporate due diligence within the EU and beyond. The EU appears determined that the Directive will have a de facto global reach, in close interaction and alignment with the OECD Guidelines for Multinational Enterprises on Responsible Business Conduct (June 2023)2 on the mechanics of due diligence.

The CSDDD requires companies to identify, prevent and mitigate potential adverse human rights impacts and adverse environmental impacts. Towards this, companies must:

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1 The Parliament opinion suggests a phasing-in between three to five years after the entry into force of the Directive, depending on company size (proposed Article 30(1)(2)).
2 See the various references to the OECD Guidelines in the Parliament opinion (eg Recitals 5, 6, 12, 16, 22, 37, proposed Art. 9(4b), 13(1a), 14(4)(a)) that aim at ensuring coherence.
A. Develop and implement a due diligence policy, spelt out in a code of conduct and to be reviewed and updated continuously (Art. 5);
B. Identify the potential or actual adverse impacts that their business operations, subsidiaries and business relationships may have on human rights and the environment (Art. 6);
C. Prevent or mitigate adverse impacts on human rights and the environment, e.g. through a prevention action plan, contractual provisions ensuring compliance down the value chain (‘contractual cascading’), investments and training for SMEs or other means (Art. 7);
D. Bring to end actual adverse impacts on human rights and the environment, e.g. by changes in the business operations, contractual provisions, tighter verification or – as last resort – the suspension or termination of supplier relations (Art. 8);
E. Establish a non-judicial notification and complaint procedure through which individuals, unions or NGOs can issue complaints regarding adverse human rights and environmental impacts (Art. 9);
F. Ensure continuous monitoring of their operations, subsidiaries and business relations (Art. 10) and publicly report on the matters covered in the Directive (Art. 15);
G. Develop a climate change strategy (‘transition plan’) specifying how the business model aligns with the Paris Agreement and the 1,5°C goal (Art. 15).³

Importantly, in the Commission proposal, companies are expected to carry out due diligence on their own operations, the operations of their subsidiaries, and the value chain operations of entities with which the company has an ‘established business relationship’. A ‘value chain’, as defined in the Commission proposal and further expanded in the Parliament position⁴, covers all upstream and downstream activities, including the marketing, use and disposal of products and services.

The Parliament position extends due diligence to any – also sporadic – business relationship, but in exchange stresses the principles of proportionality and the possibility for companies to prioritize the most pressing aspects of due diligence. Concretely, due diligence shall be ‘proportionate and commensurate’ to the likelihood and severity of adverse impacts as well as the companies’ own leverage and specific risk factors. Meaningful stakeholder engagement shall be part of all stages and dimensions of the due diligence process.

The CSDDD’s scope of application covers large European and non-European companies operating in the EU above certain minimum thresholds (Article 2). The Parliament suggests lowering the thresholds defined by the Commission to at least 250 employees combined with a worldwide net turnover of over €40 million for EU-based companies and a worldwide net turnover of over €150 million out of which at least €40

³ Note that the Commission proposal required only the biggest companies to establish such a plan, while the European Parliament opted to extend it to all companies.
⁴ The Parliament position defines ‘value chain’ broadly as including (i) activities related to, and entities involved in, the production, design, sourcing, extraction, manufacture, transport, storage and supply of raw materials, products or parts of a company’s product and the development of a company’s product or the development or provision of a service, and (ii) activities related to, and entities involved in, the sale, distribution, transport, storage, and waste management of a company’s products or the provision of services, and excluding the waste management of the product by individual consumers.⁵
million are generated in the EU for non-EU-based companies. The Commission initially foresaw lower thresholds for companies in ‘high impact sectors’ and it was discussed if auditing should fall into this category—the Parliament now suggests dropping such differentiation between different sectors.

While not directly included in the scope of the proposal, SMEs will be affected by its provisions in their capacity as subsidiaries, suppliers, contractors, or subcontractors to companies that are within its scope. Industry initiatives and independent third-party verification schemes will be important in supporting SMEs to adapt to the requirements of the Directive.

3. General implications of the CSDDD for sustainability systems

The CSDDD leaves considerable leeway for implementation. It does not establish new definitions of sustainability itself. Instead, it defines adverse impacts on human rights and the environment by referencing a list of international conventions in an annex. These will have to be covered in companies’ due diligence processes.

Industry schemes, multistakeholder initiatives and independent third-party verification can play a role in supporting compliance with the proposed CSDDD. Existing due diligence frameworks, such as the general and sectoral OECD Guidelines, will also be important in shaping how companies implement the new rules.

The CSDDD is the EU’s first attempt to establish a due diligence framework that combines human rights and environmental impacts. While due diligence was first developed for human rights impacts, it is less tested for environmental impacts. Combining both in the same legally mandated process could create a demand for comprehensive initiatives calibrated to these dual requirements. Moreover, the Parliament stressed that for suppliers operating in zones of weak governance (e.g. armed conflict, occupation, annexation), due diligence shall be sensitive to the context of the conflict and the framework of international humanitarian law. This might require further adjustments from existing human rights schemes and initiatives, such as establishing new metrics, indicators and practices that are attuned to zones of political conflict.

The Directive changes the state of play for more narrowly focused industry initiatives and independent third-party verification schemes. Companies that use different verification schemes or multistakeholder initiatives to conduct their due diligence on human rights and the environment might want these schemes to be interoperable and well aligned in their internal procedures, so that they function as different ‘modules’ of the overall sustainability due diligence process.

The CSDDD is complemented by other recent and pending initiatives under the ‘EU Green Deal’ that will also affect sustainability certification, such as the Conflict Minerals Regulation (2021), the recently adopted Deforestation Regulation (2023), a proposed Green Claims Directive, a proposed Regulation on products from forced labour and others. While regulators and companies have stressed the need for more policy coherence and to avoid multiple compliance costs, industry schemes, multistakeholder initiatives and
independent third-party verification can be leveraged and revised, as relevant, to be fit for purpose under different regulations.

The roles of ‘industry schemes, multi-stakeholder initiatives and third-party verification’
The Parliament’s position has further elaborated the definitions, roles and professional standards for ‘industry schemes or multi-stakeholder initiatives’ and ‘third-party verification’. In so doing, the Parliament addresses several points raised in ISEAL’s recommendations that called on lawmakers to provide such clarifications and set a high bar for performance and integrity. The Parliament text will likely be the primary reference in the Trilogue and accordingly forms the basis of the following analysis.

‘Industry scheme or multi-stakeholder initiative’ is defined in the Parliament’s position as:

’an initiative that companies participate in, which provides standards, procedures, tools and/or mechanisms, in order to support, monitor, evaluate, certify, and/or verify aspects of their due diligence, or the due diligence conducted by their subsidiaries and/or business relationships. Such initiatives may be developed and overseen by governments, industry associations, groupings of interested organisations, or civil society organisations’ (Article 3(1)(j)).

‘Independent third-party verification’ is defined in the Parliament’s position as:

‘verification of aspects of the due diligence of a company or parts of its value chain resulting from the provisions of this Directive either by an auditor or an audit firm that is approved in accordance with Article 3 of Directive 2006/43/EC or accredited in a Member State for conducting certifications, or by an independent assurance services provider as defined in Article 2, point (23), of Directive 2006/43/EC accredited in a Member State in accordance with Regulation (EC) No 765/2008 of the European Parliament and of the Council for the specific conformity assessment activity referred to in Article 14(4a) or by an independent third party that is accredited in a Member State for conducting certifications and which is independent from the company, free from any conflicts of interests, has demonstrated experience, expertise and competence in environmental, climate, and human rights matters, and is accountable for the quality and reliability of the audit or assessment, and meets the minimum standards set out in the delegated act as described in Article 14(4a)’ (Article 3(1)(h)).

The CSDDD envisages a dual role for industry schemes, multistakeholder initiatives and verification:

- To support suppliers’ compliance with due diligence requirements, i.e. act as key ‘facilitators’ used by companies to organise compliance and obtain and store a large amount of supplier-related data, such as for the implementation of a ‘prevention action plan’ (Article 7(2)(a) or ‘corrective action plan’ (Article 8(3)(b)), and identify and mitigate specific risks. Involvement in and use of such initiatives will not replace companies’ own due diligence procedures and will not exempt companies from possible liability (Parliament position, Article 22(2)(b)).
To create ‘leverage’ through collective action, foster local capability building, build synergies among and connect different actors (e.g. by providing access to a grievance mechanism), and drive long-term collaborative implementation with local stakeholders. These broader functions and roles are hinted at in the definition and preamble but are not wholly acknowledged.

The Parliament position has significantly expanded the quality control and credibility requirements for industry schemes, multi-stakeholder initiatives and independent third-party verification. These clarifications are crucial to fully internalise the implications of the CSDDD. Pillars of these quality control and credibility requirements shall be:

- **Guidance and methodology to assess industry schemes and multi-stakeholder initiatives** with regard to their scope, alignment with the CSDDD, and credibility. This shall include an assessment of transparency, governance, oversight mechanisms and accountability, building on the OECD’s alignment assessment methodology (proposed Article 14(4)(a)).

- The establishment of a **centralised and public digital platform** on which industry schemes and multi-stakeholder initiatives would be assessed, in order to foster comparability and overall quality of such initiatives (proposed Article 14(1a)).

- Specification of **minimum standards for third-party verification** through the Commission per delegated act after close consultation with all relevant stakeholders (proposed Article 14(4a)).

- Requirement for **third-party verifiers to be accredited or approved** under the EU regime for financial auditors or product safety (Art. 3(1)(h)) and, where necessary, exposure of third-party verifiers to sanctions, i.e. civil liability and administrative accountability, under national and EU law (proposed Recital 37).

In light of this, much will depend on how the Commission uses its mandate to create operational clarity on the assessment of industry and multi-stakeholder initiatives and on the minimum standards for third-party verifiers. This process will require broad stakeholder engagement to mobilize the expertise of existing networks and alliances of industry and multi-stakeholder initiatives and third-party verifiers, in particular those taking a systemic perspective on sustainability matters.

Moreover, some of the rules that regulate industry schemes, multi-stakeholder initiatives and independent third-party verification stem from other European and national legislation that are currently undergoing changes (e.g. laws on trademarks, unfair commercial practices and consumer sales, and the proposed Green Claims Directive). The impacts of these changes will need to be monitored independent of the CSDDD provisions.

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5 Such delegated acts are adopted by the Commission after consultation with groups of experts nominated by the Member States; Parliament and Council can raise objections to a delegated act.
4. The material scope of the CSDDD and its impacts for the industry schemes and multistakeholder initiatives

The CSDDD’s material scope includes both adverse human rights impacts (Article 3(c)) and adverse environmental impacts (Article 3(b)). It defines both through a list of international conventions in the annex.

- Regarding human rights impacts, Annex (Part I) comprises a list of specific prohibitions resulting from civil and economic rights and a catch-all reference to relevant UN and International Labour Organization norms. The Parliament position has added, among others, the right to a living wage for employees and the right to a living income for self-employed workers and smallholders.

- For environmental impacts, Annex (Part II) lists prohibitions coming from environmental conventions related to biodiversity, waste and the ozone layer. The Parliament position has considerably expanded and restructured this list, especially with regard to climate change (inclusion of Paris Agreement), ecosystem health (mentions of deforestation, overconsumption, degradation of land, marine and freshwater ecosystems) and waste and pollution (inclusion e.g. of UN Convention on the Law of the Seas, UN Water Convention).

The lists in the Annex will remain dynamic and the Commission will likely be granted the power to adjust it to make sure it remains consistent with the EU development around human rights and the environment (proposed Article 3(1a)). Existing industry schemes and multi-stakeholder initiatives will need to closely monitor the broad and dynamic material scope.

The references to international conventions are necessarily general and will need to be ‘translated’ and operationalised into verifiable indicators or data points. The Commission is tasked with developing ‘clear and easily understandable guidelines, including general and sector-specific guidance’, after broad stakeholder consultations. The Commission will expand its online ‘Due Diligence Toolbox’ that provides support to companies that engage in due diligence. Of particular importance will be digital tools on due diligence which the Commission shall actively promote (proposed Recital 46a).

Until such Commission guidelines are fully developed, industry schemes and multistakeholder initiatives might have to consider on their own how to translate the CSDDD into implementation frameworks. Being among the first-movers could offer considerable opportunities for visibility and market share. There should also be opportunities for such schemes and initiatives to clarify if their ‘translation’ of the conventions will be acceptable under the CSDDD, for example by consulting informally with the European Commission. However, in the absence of clear secondary guidance, there is a considerable risk that they could formulate insufficient standards in translating international conventions.

5. Non-judicial notification and grievance mechanism under the CSDDD
The CSDDD draws on various mechanisms for enforcement, ranging from informal complaints to administrative sanctions and civil liability. Article 9 sets an expectation on companies to set up or participate in a private notification and non-judicial grievance mechanism. These mechanisms will allow affected individuals, trade unions or other workers’ representatives and civil society organisations to raise complaints regarding actual or potential adverse human rights or environmental impacts concerning a company’s operations or those of its subsidiaries or value chain.

Currently, such mechanisms are largely non-existent, and companies will be actively looking for templates for developing them. The CSDDD itself gives very few concrete parameters for their establishment. The Parliament position explicitly adds the possibility of ‘collaborative arrangements, including industry initiatives, with other companies or organisations, by participating in multistakeholder grievance mechanisms or joining a global framework agreement’ (proposed Article 9(1)).

Here, industry schemes, multistakeholder initiatives and third-party verification can offer valuable experience and practical building blocks coming from complaint procedures around certification decisions. For instance, ISEAL is closely working with its members to draw good practices, lessons and challenges from their complaint mechanisms. Potential opportunities could include a company establishing a joint complaint mechanism with an industry scheme, or a multistakeholder initiative (or network like ISEAL) supporting in administering complaint procedures for multiple companies, for example in a specific given sector.

In the Trilogue, a well-functioning complaint procedure under Article 9 might emerge as an alternative to expanding the civil liability of companies. As the latter continues to face considerable political opposition, especially from trade associations and the conservative political spectrum in the European Parliament, who fear an increase in large damage claims against companies. Complaint procedures might then become even more prominent within the CSDDD.

Given that the CSDDD sets very few requirements for the design of such procedures, it is possible that some Member States will move ahead with more detailed provisions in their national transposition of the Directive. Such a regulatory patchwork would limit the practical viability of transnational multi-stakeholder initiatives handling joint complaints. Keeping procedures largely harmonised at the European level would allow for transnational solutions.

7. Conclusion and recommended actions

The CSDDD will set a new era for corporate and value chain governance with due diligence at its heart. This has profound implications for industry schemes, multi-stakeholder initiatives and third-party verification. They will have a particular role to play and support in the implementation of the CSDDD at multiple levels:

- As tools to verify compliance by suppliers and enable the flow of information on sustainability-related matters along the value chain (‘compliance logic’)

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• As inspiration for a collaborative and forward-looking interpretation of due diligence that is sensitive to long-term development and capability building along the value chain (‘sustainability logic’)
• As the institutional backbone and source of best practices for the new notification and complaint mechanisms to be established under the CSDDD

Providing these functions in the context of CSDDD would require high standards of credibility and organisational accountability on behalf of verification schemes and multistakeholder initiatives. The significant role of industry schemes, multi-stakeholder initiatives and independent third-party verification (which may be amplified further through secondary guidance by the Commission) will entail increased responsibility, as well as (even) greater scrutiny from external stakeholders.

With the finalised text of the CSDDD expected in late 2023 or early 2024, the question of how to position and adapt industry initiatives, multi-stakeholder initiatives and independent third-party verification schemes cannot yet be addressed in any definite sense. In the interim, they might want to carry out a preliminary assessment of:

• How their principles, requirements and criteria align with both the material scope of the CSDDD (Annex of the Directive) and the process of due diligence
• Which risks, actors or materials in the supply chain are not covered by the system or standard (e.g. uncertified or uncontrolled material entering the supply chain)
• Integrity risks in the assurance system and the system’s ability to provide information or contractual assurance about mitigation and remediation of human rights and environmental risks.