

## **New E.U. Measure on Environmental and Human Rights Due Diligence Has Far-Reaching Implications for Companies Operating in Europe and Beyond**

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On March 10, 2021, the European Parliament approved a legislative measure by an overwhelming 504-79 majority that paves the way for a landmark set of regulations setting a corporate duty of care regarding environmental protection and sustainability, internationally recognized human rights principles, and good governance practices – collectively referred to as ESG standards. Although the Parliament’s measure is not legally binding, it is expected that the European Commission will adopt regulations in general accordance with Parliament’s legislative measure by the end of the year.

These regulations will likely require both small and large companies operating in the European Union to respect human rights, protect the environment, and comport with ethical business practices in their operations and supply chains, including through their direct commercial partnerships with other business entities and suppliers. U.S. companies as well as others based outside the European Union, but that operate within the European Union would very likely also be subject to comprehensive ESG-related due diligence requirements.

By calling for a binding set of due diligence requirements, the E.U. Parliament recognized that “voluntary due diligence standards have limitations and have not achieved significant progress in preventing human rights and environmental harm and in enabling access to justice.”

### **Proposed Requirements**

The E.U. Parliament’s measure calls for companies with business activities in E.U. markets to establish a robust corporate social responsibility due diligence strategy that would also be publicly disclosed. As part of this new framework, companies will also need to prevent and/or remedy serious environmental and human rights harms that are identified in the course of the due diligence exercise.

The new measure also expects that companies will fully implement and enforce their commitments to ESG, and accordingly calls on companies to ensure that they provide adequate grievance mechanisms to human rights-holders and other stakeholders who could be harmed by a company’s activities. Furthermore, the measure calls on companies to engage with affected stakeholders through “effective, meaningful and informed discussions” when establishing and implementing their due diligence strategy.

Additional recommended enforcement measures include investigations by regulatory authorities to ensure that ESG due diligence is carried out, sanctions that can be ordered in cases where investigators find a company non-compliant, and opportunities for aggrieved stakeholders to file civil suits against companies that fail to prevent and meaningfully remedy harms stemming from their activities. The new legislative measure states that remediation proposals by companies do not prevent stakeholders from bringing civil proceedings in accordance with national law. In particular, victims “shall not be required to seek extra-judicial remedies before filing a claim before a court, nor shall ongoing proceedings before a grievance mechanism impede victims’ access to a court.”

The human rights component of the E.U. due diligence measure is clearly drawn in part from the U.N. Guiding Principles on Business & Human Rights (UNGPs), which are based on the principle that commercial enterprises should not cause harms to rights-holders. The UNGPs state that governments have a duty to protect human rights, while companies are strongly expected to respect human rights in their operations, activities, and supply chains. The UNGPs provide a clear framework for companies to carry out due diligence often and as early as possible and in consultation with affected stakeholders; to identify actual and potential human rights impacts associated with their commercial activities; and to remedy harms by enforcing human rights policies, closing gaps in the implementation of such policies,

and properly redressing grievances submitted through readily available, multi-channel grievance mechanisms.

With respect to the environment, the E.U. Parliament's measure states that due diligence frameworks should be aligned with the U.N. Sustainability Goals, as well as the greenhouse gas and global warming objectives of the European Green Deal and the Paris Agreement.

Importantly, the E.U. Parliament observes that adverse environmental impacts and human rights abuses are often closely interrelated. As the measure notes, "the U.N. Special Rapporteur on Human Rights and the Environment has stated that the rights to life, health, food, water and development, as well as the right to a safe, clean, healthy and sustainable environment, are necessary for the full enjoyment of human rights." The measure does not, however, provide much specific guidance for companies to use in assessing their direct environmental impacts, and any European Commission regulations would need to address this.

The new measure also calls for a ban on the importation of products into the European Union that are made with inputs from child and forced labor, or other types of modern slavery. This aligns with existing U.S. prohibitions on the import of such products. Pursuant to Section 307 of the Tariff Act, products made in whole or in part with forced labor, including prison labor and forced child labor, are blocked from entry into the United States by U.S. Customs and Border Protection. More information on how the Tariff Act was used to combat forced labor in 2020 and expectations for its use in 2021 is [available here](#).

### **Applicability**

The new measure has wide jurisdiction, applying to both large, publicly traded multinational enterprises – including all large businesses that are governed by the laws of an E.U. Member State or are established in the territory of the European Union – as well as all publicly listed small and medium-sized enterprises (SMEs), and SMEs operating in sectors that entail high human rights and environmental risks. Moreover, U.S. businesses should be aware that the measure's due diligence requirements will likely apply to businesses that sell goods or provide services in E.U. markets, even if such companies are not incorporated in the European Union.

### **Potential for Similar Regulations in the U.S.**

Currently, the U.S. has no similar due diligence requirements, although some legislative measures that would impose due diligence requirements have advanced to various stages in previous sessions of Congress. In addition to the existing forced labor prohibitions pursuant to Section 307 of the Tariff Act, Senator Marco Rubio (R-FL) and Representative Jim McGovern (D-MA) have spearheaded a bill – [the Uyghur Forced Labor Prevention Act](#) – that would impose a broad presumption that any products made with inputs from the Xinjiang Uyghur Autonomous Region in China are likely made from the forced labor of Uyghurs and other religious and ethnic minorities living in the region. This "rebuttal presumption" means that Xinjiang-derived products are likely to be banned from importation into the United States, unless a company can provide clear and convincing evidence that its products are in actuality not derived from modern slavery practices in Xinjiang. The latest version of the Act stripped out a previous human rights due diligence requirement for companies with supply chains in Xinjiang, most likely due to aggressive lobbying by large U.S. companies.

This win by companies, however, may soon be reversed. The Biden Administration has recently stated that it aims to require companies to disclose their ESG efforts in certain regulatory filings. Further details on this can be found [here](#).

The McGovern-Rubio bill is expected to become law at some point this year (an earlier version of the bill was passed in the House by an overwhelming bipartisan majority during the 116th congressional session). Given the Biden Administration's professed emphasis on human rights as a cornerstone of U.S. policy, there is some likelihood that new due diligence and disclosure requirements could be inserted into the bill, and the measure may serve as a precedent for extending U.S. corporate social responsibility compliance beyond Xinjiang. The Biden Administration's greater focus on normative human rights values may also strengthen calls from civil society for corporate ESG due diligence standards in law and regulation modeled after the new E.U. measure. Furthermore, President Biden has promised to bring the United States back into the international order, and his Administration is expected to coordinate in closer fashion with allies, particularly E.U. Member States.

The E.U. Parliament's measure also gives focus to gross human rights abuses in Xinjiang, and recommends that the Commission conduct "a thorough review" of commercial enterprises involving Xinjiang that export products to the European Union in a manner that identifies potential breaches of human rights, especially those related to the repression of ethnic and religious minorities.

The trends towards deeper human rights commitments in the European Union will place greater pressure on policymakers in the United States and other economically advantaged democracies to strengthen corporate due diligence and disclosure, and more aggressively enforce such standards. A discussion of potential SEC enforcement under the Biden Administration related to ESG is available [here](#).

## Recommendations

Companies that have already developed comprehensive ESG policies, ESG implementation and enforcement protocols, and regularly carry out tailored ESG due diligence and risk mitigation (in particular, by conducting environmental and human rights impact assessments as a project baseline and on an ongoing basis throughout the lifecycle of the project) will be ahead of the E.U regulations, and will likely find compliance relatively straightforward. In addition, these companies will have a clear business advantage insofar as competitors lacking such programs will need to spend significantly more time, money, and human capital to become compliant. Companies with few or weak ESG due diligence frameworks also expose themselves to significant reputational and legal risks at a time when consumers, shareholders, investors, public watchdog groups, activists, and policymakers are closely scrutinizing corporations and demanding that they conduct their activities in a more ethical and sustainable manner.

Given these developments, now may be the best time for companies to demonstrate their commitments to corporate social responsibility – both by developing appropriate internal policies and by implementing ESG-related due diligence activities throughout a company’s internal operations and its supply chains. The new E.U. measure, however, signifies that voluntary due diligence compliance may not remain the prevailing standard in the long run.

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