



Background: Further information on the EU Supply Chain Act and initial assessment by SwissHoldings

Executive Summary

With the final approval of the Council of the European Union to the European Parliament's version on 24 May 2024, the EU directive on corporate due diligence was adopted. The aim of the new directive is for European companies to check all their business partners worldwide for compliance with human rights and environmental standards in the future - including their indirect suppliers and the buyers of their products. Companies across Europe will have to document their efforts to ensure that there are no cases of for example child labour or environmental damage in their global supply chains. The new rules also apply to companies from third countries such as Switzerland if they generate an annual revenue of more than 450 million euros in the EU. SwissHoldings is currently analysing the impact of this new law on its members.

Current status: EU supply chain law with far-reaching due diligence obligations adopted

The new EU *Corporate Sustainability Due Diligence Directive* (CSDDD, EU Supply Chain Law or EU Supply Chain Act) adopted in May of this year contains both human rights and environmental due diligence obligations as well as requirements for a climate plan. The aim is to prevent companies' business activities in the EU from having a negative impact on human rights and the environment along the value chain within and outside of Europe. The discussion about the proposal were highly controversial until the very end. It was only thanks to the Belgian Council Presidency, which weakened the official trilogue agreement on key points (including the number of affected companies) as part of a backroom deal, that the law gained the necessary majority. However, the decision was rather close. Important EU members such as Germany withheld their consent to the proposed legislation until the end.

The EU Supply Chain Act is part of a comprehensive EU regulatory plan, which is based on the so-called "*EU Green Deal*". The aim of this reform is to fundamentally restructure the entire economic system: private capital flows are to be redirected as far as possible towards sustainable investments. This is intended to cover the huge investment requirements of the ambitious EU "climate plans", which go far beyond the resources of the public sector. The *EU Green Deal* is the basis for over 168 legislative proposals and regulations that are intended to promote sustainable economic activity - 76 of these initiatives have already been finalised and 24 are imminent.

Detailed schedule: The implementation of the new directive should take place in stages

The EU member states now have two years to transpose the new directive into national law. However, the new rules not only affect companies with headquarters in the EU, but also those from third countries such as Switzerland. The prerequisite is that they generate an annual revenue of more than 450 million euros in the EU. Implementation follows the schedule below:



Table: Schedule

Year	Event	Companies from EU member states	Companies from third countries
2024	Adoption of the CSDDD	The CSDDD was adopted by the EU member states on 24 May 2024.	
2024	Entry into force	Assuming typical EU directive procedures, the CSDDD will enter into force shortly after adoption.	
2026	Deadline for transposition into national law	The EU member states must have transposed the CSDDD into national law by this year.	
2027	Application for large companies	The CSDDD applies to companies with more than 5,000 employees and a revenue of more than 1,500 million euros.	Applies to companies with a revenue of more than 1,500 million euros in the EU
2028	Application for medium-sized companies	The CSDDD applies to companies with more than 3,000 employees and a revenue of more than 900 million euros.	Applies to companies with a revenue of more than 900 million euros in the EU
2029	Application for medium-sized companies	The CSDDD applies to companies with more than 1,000 employees and a revenue of more than 450 million euros.	Applies to companies with a revenue of more than 450 million euros in the EU

Source: [https://www.europarl.europa.eu/RegData/seance_pleniere/textes_adoptes/definitif/2024/04-24/0329/P9_TA\(2024\)0329_EN.pdf](https://www.europarl.europa.eu/RegData/seance_pleniere/textes_adoptes/definitif/2024/04-24/0329/P9_TA(2024)0329_EN.pdf)

New obligations: The due diligence obligations are based on the UN and OECD requirements

The companies covered by the EU directive are obliged to carry out risk-based, human rights and environmental due diligence in their operations and their value chain. In line with the new OECD requirements, the CSDDD introduces a comprehensive definition of the "chain of activities" that includes both upstream and downstream business partners. This extended chain includes all processes associated with the planning, extraction, procurement, production, transport, storage and delivery of raw materials and finished products. In addition, all phases of product development and marketing are covered by the regulation, whereby indirect suppliers and service providers are also included in the due diligence obligations.

In principle, the due diligence obligations of the EU Directive comprise six steps. They follow the OECD Due Diligence Guidance for Responsible Business Conduct, which includes due diligence measures for companies to identify and address adverse impacts on human rights and the environment.

1. Embed responsible business conduct into policies and management systems
2. Identify and assess adverse impacts in operations, supply chains and business relationships
3. Cease, prevent or mitigate adverse impacts
4. Track implementation and results
5. Communicate how impacts are addressed
6. Provide for or cooperate in remediation when appropriate

In addition, climate targets must be disclosed for 2025 and in 5-year increments up to 2050, considering the reduction targets for Scope 1, Scope 2 and Scope 3 emissions where applicable. Companies are also obliged to draw up a transition plan to combat climate change. The plan must be updated every 12 months and must include a description of the progress the company has made in achieving the defined targets.

Regarding sanctions, the Directive provides for revenue-related fines, whereby the amount of these fines and the competent national authority will have to be regulated more specifically by the individual countries as part of national implementation. The design of any new civil liability standard, for which the Directive leaves room for manoeuvre, is also to be determined at this level.

Outlook: The EU Green Deal remains active, but the enthusiasm of 2019 has been replaced by a more pragmatic approach

At the end of June this year - after the EU elections - the heads of state and government of the European Union adopted the EU's direction and objectives for the period 2024-2029. This Strategic Agenda serves as a guideline for the work of the European Council and as an orientation for the EU institutions. The Agenda is the result of a collaborative process led by the President of the European Council and includes discussions and joint decisions. In the newly adopted agenda (see also table below), the topics of "climate and sustainability" are no longer among the top strategic priorities. Instead, the focus is on maintaining the Union's competitiveness and the importance of reducing the bureaucratic and regulatory burden at all levels has been emphasised.

Table: Overview EU Strategic Agenda

<u>EU Strategic Agenda 2024-2029</u> Strategic priorities	<u>EU Strategic Agenda 2019-2024</u> Strategic priorities
<ul style="list-style-type: none"> - A free and democratic Europe - A strong and secure Europe - A prosperous and competitive Europe 	<ul style="list-style-type: none"> - protecting citizens and freedoms - developing a strong and vibrant economic base - building a climate-neutral, green, fair and social Europe - promoting European interests and values on a global stage

Sources: linked directly in the table

SwissHoldings assessment: No blind copying of EU regulation in Switzerland

Many Swiss companies that operate in the EU will be directly affected by the provisions of the new EU directive once they reach a certain size because of the third country regulation. It is therefore important to closely monitor the transposition of the directive into national law. For its part, Switzerland should take a holistic view as part of its regulatory endeavours. There is no doubt that there is a need for compatibility with EU regulations. However, it is important to make targeted and practical adjustments that are tailored to national needs. Just over 50 per cent of Swiss exports currently go to countries outside the European Union. Developments in the area of ESG regulation (environmental, social and governance) have also been dynamic worldwide in recent years. However, neither Switzerland nor other jurisdictions outside the EU have taken such a centralised (or to some extent even planned economy) approach as pursued by the *EU Green Deal*. There are even opposing tendencies in some cases. For example, the US Securities and Exchange Commission (SEC) recently delayed a further expansion of the climate reporting rules for listed companies. To avoid diverging or even conflicting requirements, it is crucial that harmonisation is not carried out exclusively with the new EU rules, but rather with the globally applicable approaches and standards.

It is also important to observe the specific impact that the new strategic priorities adopted at EU level will have on the implementation of the new directive in the member states and whether the EU will even recalibrate the EU Green Deal to some extent.

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