EURATEX

Corporate Sustainability Due Diligence

EURATEX POSITION PAPER

Recommendations:

1. Facilitate a risk-based approach and accordingly, a scope based on risk and size

2. Ensure a level-playing field through harmonisation, clarity, and better market surveillance

3. Establish clear support mechanisms for SME's and decrease burden of bureaucracy

4. Acknowledge the limits of civil liability

5. Limit Due Diligence to human rights and exclude climate mitigation

Overview

EURATEX fully appreciates and supports the importance of establishing transparent and accountable value chains. However, we believe key improvements shall be introduced for the Directive to deliver on these goals, which as it currently stands is not the case.

The current draft proposal brings the risk of heavily shifting responsibilities to smaller players in the supply chain. To avoid this, EU Due Diligence framework must uptake existing global guidelines, using a risk-based approach, i.e., the UN Guiding Principles on Business and Human Rights (UNGP) and OECD Due Diligence Guidance for Responsible Supply Chain in the Garment and Footwear Sector (OECD), scope of which should be formed on proportionate, transparent criteria, relative to companies' size and risk.

The different application of due diligence legislation across Europe is a serious risk because the proposal is a Directive and several proposal's parts entail significant room for different interpretation. This endangers the level playing field for EU companies. Harmonisation efforts should be introduced, like developing EU guidelines, and clear methodologies on carrying out due diligence, setting out precisely the scope of relevant legal actions under civil liability, and presenting more precise definitions.

To achieve concrete progress in the due diligence practices while avoiding unintended consequences, several concrete improvements shall further be applied: a mechanism to support SME's and avoid disproportionate complexity, namely the bureaucracy that companies may find themselves requiring to manage, and civil liability to be limited to Tier 1, which is the level where actions can actually be better controlled.

Climate mitigation efforts currently introduced in the draft proposal, go far beyond the framework of original due diligence. European Due Diligence should focus exclusively on human rights as protected by the UNGP guidelines.

Recommendations:

1. Facilitate a risk-based approach and accordingly, a scope based on size and risk

The industry stresses the need for European Due Diligence regulatory framework to be based on guidelines that have been consistently taken up by EU companies, namely through the UNGP and OECD guidelines.

The present proposal introduces requirements to apply actions based on "relationships" putting forward a new unknown concept, which brings the risk of heavily shifting responsibility from lead companies onto their business partners.

A risk-based approach enables companies to conduct adequate analysis of their own human rights and environmental risks, and how those risks could potentially materialise or affect their suppliers. This gives the opportunity to define which are the priority areas of the company and build up the internal due diligence framework. Additionally, it allows to focus on results and dialogue with stakeholders rather than engage in a tick-box exercise to do due diligence.

Flexibility in setting up due diligence would complement a risk-based approach. With flexibility, the risk of falling into a purely procedural obligation could be avoided. EURATEX favors an approach based on continuous improvement, encouraging innovation and proactive behaviour, discouraging narrow and compliance-orientated processes.

We further support a transparent, well-argued, and fair due diligence approach for all industries. In this regard, a line should not be drawn between one sector and another, rather all value chains should ensure to uptake due diligence based on size and risk. The scope should then be the same for all industries. The choice to include mid-cap companies (e.g. those employing between 250 and 500 employees) that operate in the so called high-impact sectors, as constituted per OECD guidelines, is disproportionate and methodologically inconsistent. There are sectors that are resource intensive and associated with human rights risks, for which OECD guidelines do not exist and thus, are not presented in the draft proposal.

Also, contractual relationships in foreign trade are of long term nature, therefore, sufficiently long transition periods (at least 4 years) for all companies in scope need to be set up to develop the corresponding systems and processes to carry out due diligence.

EURATEX reiterates that transparent, objective, and comprehensible criteria should be utilised to set the scope of European Due Diligence, that is equal for all sectors

and determined by risk and size.

Temporary agency workers are considered to have no employment relationship between the user company, usually they are not paid by the user company and thus, should not fall to be included in the calculation of the scope of the number of employees in the same way as part-time and full-time employees of the user company.

Also, the designation of legal or natural person as authorised representative in the EU by third countries (Article 2(2)) would create an additional administrative and financial burden for European companies from non-EU Member States (Switzerland, Turkey etc.) compared to countries within the EU. It is highly recommended to soften that obligation, by limiting this requirement to companies from third countries with B2C business relations (since the good is directly handed out to the end-consumer) and to exempt foreign companies with B2B business relations.

Suggestions for improvemensts:

◆ **Introduce a risk-based approach**, where risk management drives the actions by companies and not only findings of audits reports and focuses on continuous improvement.

◆ Following risk-based approach principles, **define scope that is equal for all industries**, proportionate, and based on size and risk.

◆ Capture the nature of the process that human rights due diligence is, allowing **flexibility** and not for a static box-ticking exercise.

◆ Incentives for good performance in due diligence should be provided and more **emphasis on learning-orientated approach** based on engagement and support should be given.

◆ Guarantee the introduction of **guidelines** on how to fulfil due diligence by indicating so in Article 13. Ensure that guidelines are not reinvented, but rather aligned with OECD/UNGP guidelines.

2. Ensure a level-playing field through harmonisation, clarity, and better market surveillance

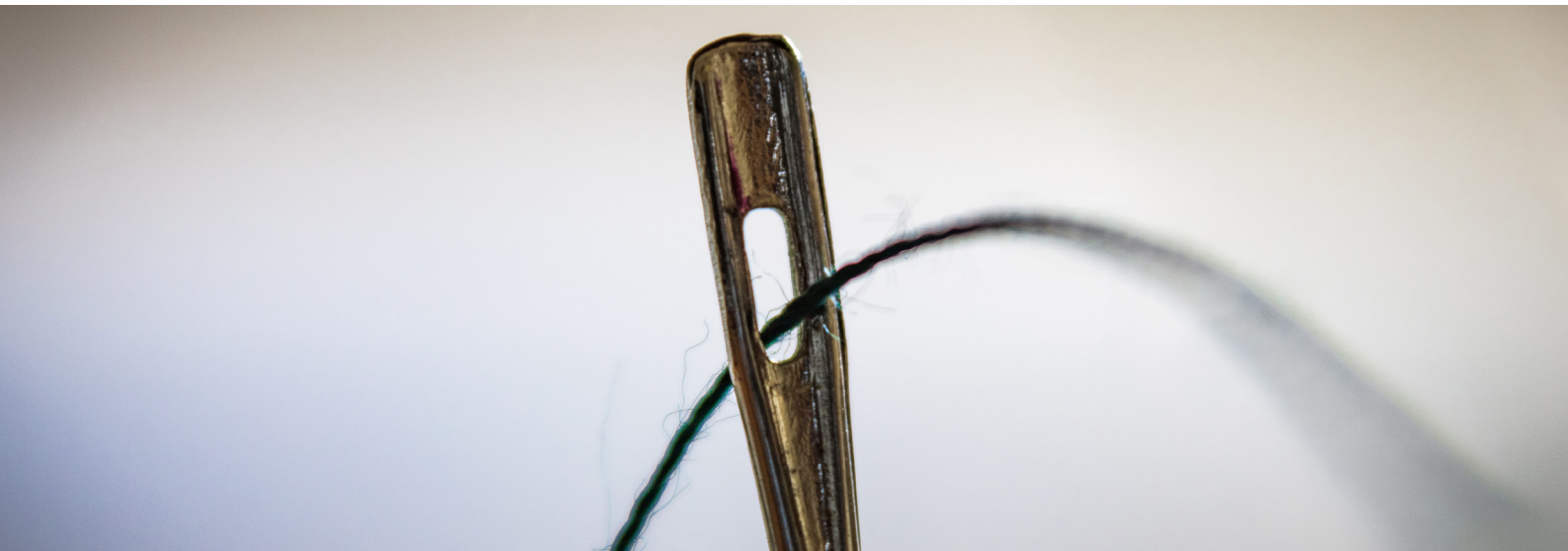
The European textiles industry emphasises the need for harmonisation of requirements, common rules, and common understanding and definitions of responsible company conduct, due diligence, sustainability etc.

The current proposal includes no provisions that limit the faculty of Member States to legislate beyond the provisions of the proposal, this increases the likelihood of further fragmentation on requirement across the Union and seriously affects the level playing field of companies in the EU. The variety of new legal vague terms without established methodologies can lead to a myriad of interpretations, requirements and implementation processes, leading to unequal conditions of competition within the EU.

For European companies to remain competitive at a global level, and at the same to promote sustainability and human rights in an impactful manner, the legislative framework needs to be harmonised between Member States. High complexity in terms of administration and procurement of documents for compliance for companies is feared. Clarifications and limitations are paramount to attain harmonisation.

At the same time, the EU regulatory framework for due diligence cannot be isolated from the existing or in-the-making European climate and environmental policies. Coherence with other EU due diligence measures (adopted or ongoing) is paramount to avoid duplication.

In particular, effective EU market surveillance to verify compliance of third-country companies will be central to achieve level playing field. In addition, a proper monitoring and enforcement mechanism should work equally for each EU member state with an integrated data framework and unique reporting at EU level.



Suggestions for improvemensts:

◆ Limit the usage of "should" to provide more **certainty**. Following risk-based approach principles, define scope that is equal for all industries, proportionate, and based on size and risk.

◆ Present more precise wording to **limit interpretation**, by providing examples of: established business relationships, reasonable terms, fair terms, reasonable grounds, appropriate measures, administrative sanctions, triggering of civil liability.

◆ Introduce more **definitions** on: indirect/ direct partners, legal entity.

◆ Develop **methodologies/guidelines** for: preventing and mitigating adverse human and environmental impact, identifying actual/ potential adverse impacts, procedures for complaints, for setting up, overseeing due diligence, clarifying whether conducting due diligence is necessary for all risks listed in the Annex, or whether companies could assess which to prioritise in accordance to their own risk assessments. Concept of prioritisation and proportionality of actions should have a more central role in the Directive, as expressed in existing guidelines (UNGP and OECD). These could be introduced in EU due diligence guidelines as mentioned in Article 23.

◆ Specify **suitable industry initiatives** for verification of compliance with contractual assurances.

◆ Set **minimum criteria** after which should be possible to lodge a complaint and institute a step in the procedure that allows for relevant parties to hold an informal dialogue before a legal procedure may be launched preventing companies from long and costly processes, for example by the grievance mechanisms indicated in OECD/ UNGP guidelines. This procedure could also be facilitated with the national OECD contact points and could be clarified in EU due diligence guidelines as mentioned in Article 23.

◆ Ensure that the **European Network of Supervisory Authorities** exchanges on actions for the purpose of carrying out harmonising efforts.

◆ Set out a clear scope of the relevant legal actions under **civil liability**, by defining who can bring a relevant legal action before the relevant court (i.e. a right to action) and under which circumstances. The right balance must be found between enabling the access to justice or a right to remedy and reaffirming the principles of the burden of proof (the presumption of innocence) of business.

◆ Introduce coherent **director's duty of care**. As the proposal stands now, it presents unspecified and very far-reaching general policy goals, creating legal uncertainty about director's own actions.

◆ Introduce a monitoring and **enforcement** mechanism that works equally for each EU member state.

3. Establish clear support mechanisms for SMEs and decrease burden of bureaucracy

Although the burden on SMEs is acknowledged in the proposal, and they are removed from scope, SMEs will certainly be indirectly affected by this Directive through business relationships with those companies in the scope and their 'code of conduct'. In the absence of clear support mechanisms, harmonised across the EU, the level playing field will be affected potentially up to termination of contracts for reasons beyond the control of SMEs (e.g. inability to follow code of conduct).

It should be considered that in case the value chain or large parts of it lies exclusively within the EU, textiles human rights due diligence, and certainly not only textiles, in the EU/EEA already follow strict corporate responsibility. Verification within EU/EEA of due diligence is certainly necessary, but the monitoring that is expected under the proposal in the EU/EEA would create an immense bureaucratic burden to EU textiles industry, highly represented by SME's.

Thus, exemptions from liability for established industry-specific standards ("safe harbour") need to be recognised. Self-declarations lists based on the tried-and-tested model of the existing EU export control legislation, or "EU Green Lists" could also contribute to legal certainty and feasibility. Countries where a high level of legal standards already exist and law enforcement is guaranteed, like in the EU/EEA, similarly to the concept introduced for deforestation-free products could make up these lists, exempting them from due diligence procedures. This would avoid bureaucracy, simplify and shorten the process, especially for SMEs.

Additionally, emphasis must be placed on the need for various reporting obligations to be kept to an absolute minimum. Standardisation and simplification with regard to reporting obligations must be continued so that companies are protected from being overburdened in the long term. There must also be more transparency when working out the individual details of a reporting obligation and the companies should be adequately consulted.

Another approach for exemptions would be the existence of free trade agreements with the EU, especially since sustainability issues are increasingly addressed there. With those countries which Europe has FTA with, it would be redundant to require companies to extensively report on their environmental-social behaviour. In principle, such an FTA should already ensure a sustainability framework.

Suggestions for improvemensts:

◆ Measure the **support** that will be necessary for **SMEs**.

◆ Work with industry on **guidances** and capacity building for supply chain partners.

◆ Ensure all-encompassing **harmonised** support mechanisms for SME's across the Union i.e. harmonised financial aid, trainings by introducing these in the proposal.

◆ Facilitate companies' compliance by **safe harbour** provisions and positive/negative lists, e.g. following the example of the already existing EU export control law.

◆ **Reporting** obligations must be kept to a minimum, usage of **standards** should be continued and companies should be consulted on these obligations.

4. Acknowledge the limits of civil liability

The European textiles industry understands the need for companies in scope to engage with players in their value chain through risk-based due diligence approach, and that support to these players is a salient requisite as well. Civil liability, however, must be limited to cases where damage is attributable and foreseeable as a result of the company's own actions. In this regard, the imposition of sanctions must be clearly limited to intentional and grossly negligent violations.

Including the entire value chain of a company would lead to uncontrollable obligations and unforeseeable risks. The introduction of responsibility for actions by third parties - i.e. indirect suppliers or resellers would be a rare exception in European and international legal systems, also diverging from existing due diligence guidelines.

Thus, corporate duty of care and contractual liability should only extend to the

direct suppliers ("Tier-1"), the level that can actually be controlled. It is heavily challenging for a company to control its whole value chain, upstream (supplier side) as well as downstream (e.g. clients, retailers). This would also result to be more efficient as it stands in line with other national mandatory frameworks (e.g. France, Germany, etc.).

An introduction of a clearly and legally defined definition of the supply chain is additionally instrumental, the depth of which should absolutely be limited to the level of the direct supplier ("Tier 1"). While, if the buyer level of a company is also to be included, a clear definition is required that excludes private consumers from the group of buyers to be monitored.

Suggestions for improvemensts:

- Introduce a clearly and legally defined definition of the supply chain, the depth of which is limited to the level of the direct supplier ("Tier 1").
- Limit legal liability to business relationships where companies have one direct contractual relationship (Tier-1).
- Limit the imposition of sanctions to intentional and grossly negligent violations.

5. Limit Due Diligence to human rights and exclude climate mitigation

The industry supports the Paris Agreement and the objectives of climate-neutrality by 2025. However, the requirement to adopt a plan that ensures business models and strategies are compatible with transition to a sustainable economy, following Paris Agreement principles, goes far beyond the framework of original due diligence.

Suggestions for improvemensts:

- European Due Diligence should focus exclusively on human rights as protected by the UNGP guidelines.

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About EURATEX

As the voice of the European textile and clothing industry, EURATEX works to achieve a favourable environment within the European Union for design, development, manufacture and marketing of textile and clothing products.

The EU-27 textile and clothing industry, with around 160,000 companies employing 1.5 million workers, is an essential pillar of the local economy across many EU regions. With over € 62 billion of exports, the industry is a global player successfully commercializing high added value products on growing markets around the world.

Working together with EU institutions and other European and international stakeholders, EURATEX focuses on clear priorities: an ambitious industrial policy, effective research, innovation and skills development, free and fair trade, and sustainable supply chains.

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