COMMENTS ON THE TEXTS ADOPTED BY THE COUNCIL AND THE PARLIAMENT ON THE PROPOSAL FOR THE CORPORATE SUSTAINABILITY DUE DILIGENCE DIRECTIVE

July 2023

Eumedion is supportive of the objectives of the European Commission's proposal for a corporate sustainability due diligence directive (hereinafter: directive). We are a proponent of ambitious European legislation in the area of corporate sustainability due diligence since it fosters responsible business conduct throughout the whole value chain. In light of the trilogue, Eumedion, representing the interests of institutional investors who have more than € 8 trillion assets under management and who invest in almost all European listed companies, would like to make some comments on the positions of the European Parliament and the Council.

THE THRESHOLDS FOR APPLICATION SHOULD BE ALIGNED WITH THE CSRD, BUT A LOWER THRESHOLD FOR HIGH-RISK SECTORS IS PREFERRED

- Eumedion is in favour of optimal alignment between the European sustainable finance legislative initiatives and the interlinked requirements stemming from these initiatives. This means that the primary thresholds (in terms of number of employees and turnover) for application of the directive should be aligned with the CSRD, with requirements being applied by (parent) undertakings within the meaning of CSRD. Additionally, Eumedion is of the opinion that a lower threshold specifically for high-risk sectors is preferred. Therefore support for the Council's text on art. 2(1) (b).

COMPANIES SHOULD DEVELOP AND IMPLEMENT CLIMATE TRANSITION PLANS

- We believe that companies should prepare a climate transition plan in order to operate completely climate-neutral by 2050 at the latest. The transition plan must contain short-, medium- and long-term CO2 emission reduction targets and explain how the company intends to achieve these targets. Therefore support for the Parliament's text on art. 15.

DIRECTORS' DUTIES SHOULD BE COVERED BY THE DIRECTIVE

- Eumedion is of the opinion that directors of companies should take into account the consequences of their decisions for sustainability matters when fulfilling their duty to act in the best interest of the

company. This includes, where applicable, human rights, climate change and environmental consequences, in the short, medium and long term.

IT SHOULD BE POSSIBLE TO PRIORITISE ADVERSE IMPACTS

- With respect to addressing adverse impacts in the supply chain, Eumedion prefers to introduce the concept of prioritisation based on severity and likelihood of the adverse impact. Therefore we support the Council's text on art. 6a and the Parliament's text on art. 8b.

ADVERSE CLIMATE IMPACTS SHOULD BE INCLUDED FROM THE OUTSET

- Adverse climate impacts pose an immediate issue that requires a firm focus. Eumedion believes that these impacts should be included in the due diligence requirements from the outset rather than leaving this subject to review in only seven years' time as proposed by the European Commission. Therefore we support the Parliament's text on art. 29 (1) (d).

REGULATORY OVERLAP FOR THE FINANCIAL SECTOR SHOULD BE AVOIDED, WITH REQUIREMENTS SUFFICIENTLY CLARIFIED AND DELINEATED

- Eumedion believes that due diligence obligations for the financial sector contribute to achieving the goals of the directive. Notwithstanding our general support we believe that the specificities of financial services need to be acknowledged as set out in Recital 36b of the Council's text and that unnecessary administrative burden and fragmentation should be avoided.
- To fully avoid fragmentation and overlap, ideally the due diligence activities and reporting requirements for financial market participants would on the one hand be covered by the CSDDD and CSRD (for their own operations and activities involving (in)direct business relationships), and on the other hand by the SFDR (due diligence and reporting requirements regarding investments in investee companies).
- Currently, large financial market participants already need to publish a statement on their due diligence policies with respect to the principal adverse impacts of investment decisions on sustainability factors (art. 4 SFDR and chapter II of the SFDR Delegated Regulation). And institutional investors and asset managers already need to comply with obligations in the area of engagement (art. 3g SRD II). Furthermore all parties subject to AIFMD/UCITS are already required to ensure a high standard of diligence in the selection and monitoring of investments (art. 23 UCITS Delegated Directive and art. 18 AIFMD Delegated Regulation). Overlap in reporting and due diligence requirements for the aforementioned financial market participants should be avoided. Therefore we support the Council's text on art 2 (7).
- Should the European legislators decide to adopt the proposed art. 8a, then it should be made clear a) that institutional investors and asset managers have the possibility to prioritise their engagement with investee companies on the basis of the significance and scale of adverse impacts, b) that the investments of institutional investors in investee companies should not be understood as providing

financial services and that the articles relating to e.g. prevention of impacts (art. 7) and bringing to an end of impacts (art. 8) do not apply to financial markets participants in so far as the investments in investee companies are concerned, and c) that financial market participants are not directly linked to and cannot be held liable for the adverse impacts caused or contributed to by investee companies.

- Further explanations to this position are provided in below annex.

For more information:

Ron Gruijters, policy officer sustainability, tel. +31 70 2040 305; e-mail: ron.gruijters@eumedion.nl

Eumedion's registration number with the European Commission and Parliament is: 65641341034-11.

ANNEX: EXPLAINING THE POSITION ON AVOIDING REGULATORY OVERLAP FOR THE FINANCIAL SECTOR

- Eumedion believes that due diligence obligations for the financial sector contribute to achieving the goals of the directive. In order for these obligations to be effective from a sustainability impact perspective as well as actionable from a practical perspective, the proposed requirements should sufficiently take account of the specificities of and differences between the various activities and services within the financial sector, as also set out in Recital 36b of the Council's text. At the same time, given the extensive EU-legislation already in place and still being implemented by financial market participants (such as the SFDR), it is important to avoid unnecessary administrative burden and fragmentation.
- Ideally, the European legislative framework would avoid fragmentation of requirements altogether, by separating due diligence activities and reporting requirements for financial market participants on the one hand by CSDDD/CSRD (for their own operations and activities involving (in)direct business relationships), and on the other hand by SFDR, from harmonised due diligence and reporting requirements regarding investments in investee companies on the other (via SFDR). This would also eliminate the potential gap created by the Parliament proposal regarding reporting on investments in investee companies, as this is not covered by the CSRD.
- Currently, large financial market participants already need to publish a statement on their due diligence policies with respect to the principal adverse impacts of investment decisions on sustainability factors (art. 4 SFDR and chapter II of the SFDR Delegated Regulation). And institutional investors and asset managers already need to comply with obligations in the area of engagement (art. 3g SRD II). Furthermore all parties subject to AIFMD/UCITS are already required to ensure a high standard of diligence in the selection and monitoring of investments (art. 23 UCITS Delegated Directive and art. 18 AIFMD Delegated Regulation). Overlap in reporting and due diligence requirements for the aforementioned financial market participants should be avoided. Therefore we support the Council's text on art 2 (7).
- It is of fundamental importance that the introduction of a specific clause for the activities of institutional investors and asset managers is accompanied by a clause that specifies that articles relating to e.g. prevention (art. 7) and bringing to an end of impacts (art. 8) do not apply to financial markets participants in so far as the investments in investee companies are concerned. We therefore have reservations regarding the scope of the Parliament's text regarding the requirements for institutional investors and asset managers. While we strongly support a proportionate set of due diligence activities for institutional investors and asset managers, such as already introduced by SFDR and by art. 8a of the directive, the Parliament's text insufficiently takes into account the specific nature of investments by institutional investors and the way these activities by default are different from other economic activities based on direct and indirect business relationships. As the Parliament's text does not clearly define and delineate the term *financial services* and seems to include investments in investee companies, the text suggests

that the full set of due diligence obligations needs to be applied to investments in investee companies as well as to the business relationship between institutional asset owners and asset managers. This includes the identification, prevention (art. 7) and bringing to an end (art. 8) of (potential) adverse impacts in case the so-called appropriate measures introduced by art. 8a and specifically tailored to stewardship activities by institutional investors and asset managers, fall short of these requirements set by the directive. This seems to be in open conflict with the proportionality clause introduced by the Parliament's text on art. 8a (3), requiring proportional and commensurate actions by investors that take due account of the degree of control they have over investee companies. Indeed, since institutional investors generally have no business relationship with investee companies, the degree of control is by nature limited. They cannot assume the role and responsibilities of the board of a company, and in most cases they lack the possibilities of other economic agents to mitigate risks by including adequate clauses in contractual relations. However, the directive's outcome oriented requirements (set by a.o. art. 7 and 8) and potential consequences, for example in terms of terminating the business relationship, still seem to apply and therefore do not respect this distinction. In practice, this would mean terminating holdings and potentially even terminating asset management contracts by institutional asset owners. Therefore, these requirements would fundamentally affect options available to institutional investors and the investment services they require.

- Accordingly, to underline the specific nature of investment in investee companies within the scope of the directive, it should also be made sufficiently clear that such investments can never be considered 'causing', 'contributing to' or 'directly linked to' *adverse impacts*, but only as 'directly linked to' *a company* that itself may be causing, contributing to or is directly linked to adverse impacts.
- Lastly, any requirement to engage with the investee company and to exercise voting rights in order to induce the management body of an investee company to bring the actual impact to and end or minimise its extent, should also take due account of obligations already enshrined in EU-law. Currently institutional investors and asset managers already need to publicly disclose (on a comply or explain basis) an engagement policy that describes how they integrate shareholder engagement in their investment strategy (art. 3g SRD II). And large financial market participants are (among others things) already obliged to provide brief summaries of any other engagement policies to reduce principal adverse impacts, this should include a description of how those engagement policies will be adapted where there is no reduction of the principal adverse impacts over more than one period reported on (art. 8 SFDR Delegated Regulation). We believe that the aforementioned parties should continue to comply with those existing rules and it is of key importance that the directive should not apply to those institutions for their investee companies to avoid delineated regulatory overlap. Should the European legislators decide to adopt the proposed art. 8a (3) then it should be made clear that institutional investors and asset managers have the possibility to prioritise their engagement with investee companies on the basis of the significance and scale of adverse impacts.