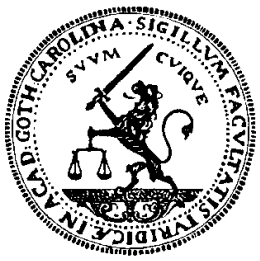

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Mandatory Human Rights Due Diligence

A study on sources of international business and human rights law, and stakeholder engagement in the context of the EU's sustainability due diligence directive

JURM02 Graduate thesis

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Summary

The European Council's proposal for a corporate sustainability due diligence directive (the "Proposal") aims to introduce obligations and responsibilities for some companies ("Company/Companies") related to sustainability matters. Part of the reasons for the Proposal was the emergence of global value chains, which are prone to contain human rights violations. The model for the Proposal was the United Nations Guiding Principles on Business and Human Rights ("UNGP") which promotes business and human rights by means of soft law.

This paper investigates the business and human rights hard law embedded in the proposed directive, and in a broad context investigates if hard law is necessary for the promotion of business and human rights. The conclusion reached is that soft law can become binding on companies by means of voluntary participation, however, the voluntarism limits effective enforcement and supervision of wide-spread responsible business conduct. Hard law is therefore necessary for the enforcement of sustainable business practices, but the promotion of the proposed hard law came in the form of model soft law, meaning that hard law is not key to promoting business and human rights, rather that soft and hard law are complementary. Based on the foregoing, the paper also discusses what role human rights soft law ought to have in the context of emerging hard law. Since soft law facilitates the promotion of business and human rights, and hard law facilitates effective enforcement, the two should not diverge on central terms and principles, since that may curtail the evolution of a harmonised global standard for responsible business conduct.

Three provisions from the Proposal related to stakeholder engagement are investigated in the paper. These relate to (i) the definition of direct and indirect business partners, (ii) providing targeted support to business partners to help adherence to a prevention action plan and, finally, (iii) termination of business relationships. The provisions provide for a balanced set of tools for Companies in their due diligence regimes. There is however a degree of uncertainty and potential limitation in the practical application of the measures enumerated. What differentiates a direct business partner from an indirect business partner is whether there is a commercial agreement between the parties. The paper shows, however, that there is a risk of uncertainty as to whether a commercial agreement is entered into pursuant to responsibilities that may actualise on the part of an in-scope company. The mechanisms embedded in the Proposal risks creating uncertainties as to whether a business partner is direct or indirect and thereby obscures predictability in practice. The targeted support that an in-scope Company may have to provide to a business partner is wide in scope and allows for creative discretion and collaboration. The measures are however provided with a ceiling as to how extensive the need for assistance may be before the Company must assess whether the business relationship must be terminated. The mechanisms of termination of

partnerships are given a prominent role which has negative implications for the stakeholders in a business partners operations since termination is ultimately unsatisfactory engagement pursuant to its inherent inability to resolve a potential adverse impact.

Sammanfattning

Europeiska rådets förslag till ett direktiv om tillbörlig aktsamhet för företag i fråga om hållbarhet (”Förslaget”) syftar till att införa skyldigheter för vissa företag (”Företag/Företaget”) relaterat till hållbarhet. Ett av skälen till Förslaget var framväxten av globala värdekedjor, som tenderar att ge upphov till kränkningar av mänskliga rättigheter. Förlagan till Förslaget var Förenta nationernas vägledande principer för företag och mänskliga rättigheter (”UNGP”) som även de syftar till att främja frågor om företagande och mänskliga rättigheter (”hållbart företagande”), men istället för positiv rätt (”hard law”) så använder UNGP en mix av bland annat moraliska, ekonomiska och, till viss del, även bindande källor som samverkar för att skapa normativ vägledning (”soft law”).

Denna uppsats undersöker den lagstiftning som eventuellt tillkommer genom det föreslagna direktivet, och i ett vidare sammanhang även huruvida hard law är nödvändigt för att främja hållbart företagande. Utredningen visar att soft law kan bli bindande för företag genom frivilligt deltagande, men frivilligheten begränsar effektivt genomdrivande och upprätthållande av mer omfattande hållbart företagande. Hard law är därför nödvändigt för genomdrivande av hållbart företagande i stor omfattning, men främjandet av detsamma har soft law redan demonstrerat en förmåga till. Detta innebär att hard law inte är en nödvändig förutsättning för att effektivt främja hållbart företagande, och det visar även att soft law och hard law kompletterar varandra.

Med grund det som anförts ovan diskuterar uppsatsen även vilken roll soft law borde ha i framväxten av hard law. Eftersom soft law främjar framväxten av hållbart företagande, och hard law främjar effektivt genomdrivande av detsamma, bör de två inte avvika från varandra beträffande centrala principer eller materiell begreppsanvändning. Divergerande utveckling riskerar att hämma harmoniserad utveckling av globala standarder för hållbart företagande.

Tre bestämmelser från Förslaget som behandlar Företags engagemang i sina intressenter kommer utredas. En intressent kan vara exempelvis anställda i ett Företags egna verksamhet eller i en affärspartners verksamhet. Bestämmelserna gäller (i) direkta och indirekta affärspartner, (i) riktat stöd till affärspartners som behöver hjälp med att uppfylla kraven i en förebyggande handlingsplan och, slutligen, (iii) avbrytande och avlutande av affärsförbindelser. Bestämmelserna ger Företag en balanserad uppsättning verktyg för att kunna utöva tillbörlig aktsamhet. Det finns emellertid vissa begränsningar och osäkerheter kring tillämpningen av dem. Skillnaden mellan en direkt och indirekt affärspartner består i att det finns ett affärsavtal mellan ett Företag och dess direkta affärspartner.

Uppsatsen visar att det inte är helt klart om ett affärsavtal ingås när Företag vidtar åtgärder för att uppfylla sina skyldigheter gentemot sina affärspartners i enlighet med Förslagets bestämmelser. De mekanismer som byggts in i Förslaget riskerar att tillsammans skapa osäkerheter kring huruvida en affärspartner är direkt eller indirekt vilket får konsekvenser för både Företag och deras affärspartners. Främst påverkar osäkerheten Företag eftersom en direkt partner har utvidgade rättigheter gentemot Företag, och osäkerheten innebär att indirekta affärspartners tillsynes kan kvalificeras om till direkta affärspartners utan att det varit lagstiftarens avsikt. Det riktade stöd som ett Företag kan behöva ge till en affärspartner är omfattande men proportionerligt och möjliggör kreativ problemlösning och samarbete. Det finns emellertid andra bestämmelser som inverkar på hur omfattande behovet av stöd får vara innan mekanismer för avslutande av affärsförbindelser träder in. Mekanismerna för avslutande av affärsförbindelser ges en framträdande roll vilket kan få negativa konsekvenser för utsatta intressenter i en affärspartners verksamhet eftersom avslutande av affärsförbindelser inte bemöter eller löser en potentiellt negativ effekt.

Abbreviations

UNGP	United Nations Guiding Principles on Business and Human Rights
Guiding Principles	United Nations Guiding Principles on Business and Human Rights
UN	United Nations
EU	European Union
CSR	Corporate Social Responsibility
HRDD	Human Rights Due Diligence
CSDDD	Corporate Sustainability Due Diligence Directive
SRSG	Special Representative of the Secretary-General on the Issue of Human Rights and Transnational Corporations and Other Business Enterprises
OECD	Organisation for Economic Co-operation and Development
NCP	National Contact Point
WSRN	Worker-Driven Social Responsibility Network
The Commission	The European Commission
The Council	The European Council
OHCHR	Office of the United Nations High Commissioner for Human Rights

1 Introduction

1.1 Background

The large gaps in labour wages between economically developed and developing countries have made the separation of production processes (*e.g.*, shipping products overseas for processing and then back again or to another stage in the production process) profitable as opposed to the traditional method of bundling the process in one region or factory.[1] These wage gaps were one of contributing factors which made global supply chains profitable, and the development of the information and communication technology made them possible and more manageable.[2]

It is in these systems of international corporate operations with sprawling supply chains that human rights violations tend to occur, and in some countries human rights violations are a part of local business models.[3] One of the most anticipated pieces of legislation aimed at combating the human rights violations in global supply chains is a sustainability due diligence directive, which aims to introduce legal obligations for certain companies to implement due diligence measures to identify, prevent and remedy adverse human rights impacts.[4]

The legislative proposal was first adopted by the Commission (the "Commission's draft"),[5] and most recently the Council adopted its General Approach (the "Proposal").[6] The Proposal has been anticipated for some time but has also gained critique for being too burdensome to the extent that it negatively impacts the competitiveness of EU companies,[7] while at the same time being criticized for not being wide enough in scope, or too loose with its definitions.[8] The contention presented above raises questions as to whether the measures and scope embedded in the Proposal provides the people vulnerable to adverse impacts with means to be seen by the companies that will be obligated to perform the due diligence, in this paper referred to as "stakeholder engagement". The Proposal is rooted in business and human rights soft law, in particular the United Nations Guiding Principles on Business and Human Rights (the "UNGP" or "Guiding Principles"), the OECD Guidelines for Multinational Enterprises ("OECD Guidelines") and the OECD Due Diligence

[1] Elms & Low (2013) page 16.
[2] Elms & Low (2013) page 16.
[3] LeBaron (2020) page 40.
[4] Just and sustainable economy: Commission lays down rules for companies to respect human rights and environment in global value chains, European Commission (2022), Accessed 20 May 2023.
[5] Proposal for a directive on Corporate Sustainability Due Diligence and amending Directive (EU) 2019/1937 to the European Parliament.
[6] Proposal for a Directive of the European Parliament and of the Council on Corporate Sustainability Due Diligence and amending Directive (EU) 2019/1937.
[7] Haeusgen (2023).
[8] Quiroz (2022).

Guidance for Responsible Business Conduct ("OECD Guidance"). These soft law instruments provide material guidance on how a company should engage with its stakeholders to facilitate meaningful and productive communication but are not binding on companies. The debate on the nature, similarities and differences between soft law and hard law is however contentious.[9]

Soft law can become binding by way of voluntary agreements such as commercial compliance undertakings. Legally binding soft law is then enforceable, which raises the question as to why there is a need for hard law in business and human rights, especially since large companies are already adopting instruments such as the UNGP on a large scale. [10] This indicates a market willingness to adhere to established business and human rights soft law, regardless of whether it is done out of corporate altruism or because it provides them with competitive advantages.[11] Indeed, there are competitions and awards centred around corporate social and environmental efforts and achievements.[12] From the observations above emerges questions as to why hard law is emerging now, a mere decade after the introduction of the Guiding Principles, and whether business and human rights needs hard law to continue to evolve. The UNGP is just over a decade old but has already managed to greatly influence proposed legislation that will, eventually, have legal effect in the European Union. Understanding the effect soft law has on business and human rights law today may be conducive for an investigation as to what role soft law should play in the context of emerging business and human rights hard law as well.

1.2 Purpose and research questions

The purpose of this paper is to investigate why business and human rights hard law is emerging in a corporate climate that seemingly embraces the established soft law. By attempting to answer the first descriptive question, a prescriptive question regarding how soft law should influence hard law will be investigated. Finally, the matter of how well the Proposal accounts for stakeholder engagement in some of its provisions, and whether that engagement is designed to produce meaningful output, will be investigated. The purpose of the paper can be achieved by answering the following questions:

(i) Is Hard Law Necessary for the Promotion of Business and Human Rights?
(ii) What Role Should Soft Law Have in the Context of Emerging Hard Law?
(iii) Are the Provisions of the Proposal Conducive to Meaningful Stakeholder Engagement?

[9] Cerone, Gammeltoft-Hansen & Lagoutte (2016) page 1; Bosi (2021).
[10] Commission's draft, Explanatory Memorandum, page 2.
[11] Commission's draft, Explanatory Memorandum, page 2.
[12] Ponte (2019), Page 1.

1.3 Methodology and materials

The legal dogmatic method is traditionally said to be foundational for an investigation of legal sources with regards to the hierarchy of sources of law within that system, *i.e.,* investigating "what is law".[13] This will be achieved in this paper by reconstructing the contents of norms, be they binding or otherwise, against a set of questions pertaining to the application of said norms.[14] Utilizing the legal dogmatic methodology as describe above can assist in answering questions as to what rules are applicable (*de lege lata*) or which rules should be adopted (*de lege ferenda*). [15]

Because of the range of sources of law in this paper (*e.g.,* literature on human rights due diligence, economic supply chain theory, recommendations, and interpretive guidance), there is a need to escape the dichotomy of binding and non-binding law. For instance, the implications of the proposed Union legislation will be discussed and analysed against a range of contexts, and the lack of case law or definite guidelines from the bodies of the European Union will require analytical freedom. Moreover, business and human rights soft law instruments have a prominent role in this paper, and their normative value carry some ambiguity since they are authoritative and well-established among large companies while at the same time being non-binding.[16]

Using a narrow definition of legal dogmatic method as described above would therefore be impractical, since the aim of this paper is not exclusively to uncover what is and will be law, but also investigate the implications of the legal effects on both in-scope EU-companies as well as their business partners and in turn their employees. The term "legal dogmatic method" does however, contrary to the implications of the term, not revolve solely around dogmatic reinforcement of positive law. A legal dogmatic analysis instead refers to analysis of various dimensions of norms and investigations into how rules should be understood in a specific context.[17] It is also helpful to have a less strict method of analysis when attempting to answer the third research question pertaining to the Proposal's conductivity to meaningful stakeholder engagement. Based on the foregoing, the legal dogmatic analysis will be the methodological foundation for this paper.

The paper will discuss the articles of the Proposal, and its recitals will provide interpretive guidance for those discussions. The EU Interinstitutional Style Guide provides that the Preamble covers the entirety of the content between the title of the legislation and the normative provisions.[18] The recitals are part

[13] Nääv & Zamboni (2018), page 21.
[14] Nääv & Zamboni (2018), page 21.
[15] Lehrberg (2017), page 203.
[16] Cerone, Gammeltoft-Hansen & Lagoutte (2016) page 1–2; See also Commission's draft, Explanatory Memorandum, page 2.
[17] Nääv & Zamboni (2018), Page 26.
[18] EU Interinstitutional Style Guide (2022) Section 2.2.

of the preamble but do not provide legal effect.[19] They are merely tools of interpretation and are used sparingly by the European Court of Justice.[20] Even though they do not provide normative value, they are useful for interpreting the legislative acts.[21] Literature about business and human rights due diligence soft law will be used. Articles from interest organisations will be used sparingly and only to illustrate common points of contention and never as guidance on material law. The Commission's draft will provide the background to the Proposal while the Council's draft will be used to gauge the provisions *per se*. The Worker-Driven Social Responsibility Network's ("WSRN") is active in disseminating human rights due diligence by promoting meaningful engagement of stakeholders in the labour-segment of the global supply chain. Their critique of social auditing will help ground the thesis in a stakeholder-oriented perspective.

The investigation is grounded in a perspective that critically assesses available instruments for responsible business conduct centred around the interests of stakeholders in global supply chains. Available measures for making visible the most vulnerable stakeholders in global value chains are the focus of this paper. The business partners of companies within the scope of the proposed directive are therefore placed at the focal point of the paper rather than the EU-companies themselves or their subsidiaries. For the section on business and human rights soft law the focus has been the UNGP and OECD Guidance and Guidelines since they are the dominant instruments in the area and have been key in the development of responsible business conduct and eventually the Proposal.

1.4 Delimitations

There are more provisions either directly or indirectly related to stakeholder's interests than will not be covered in the paper, *e.g.,* monitoring (Article 10), communicating (Article 11), substantiated concerns (Article 19), the civil liability regime (Article 22), the complaints procedure (Article 9), the potential exclusion of regulated financial undertakings from the personal scope of the directive, and penalties (Article 20). Since the aim of this paper is to assess stakeholder engagement in the more proactive and antecedent stages of a potential adverse impact, bringing adverse impacts to an end (Article 8) will not be investigated either.

Environmental matters will not be continually represented in this paper, but I would remind the reader that the human rights due diligence presented and analysed is largely transposable to environmental matters as well, since the Proposal is devised to aim at both issues jointly. The scope of required due diligence, for instance, is the same for both environmental matters as for

[19] European Commission Service Juridique, Quality of Legislation Team (2024) page 9.
[20] European Commission Service Juridique, Quality of Legislation Team (2024) page 9.
[21] Nääv & Zamboni (2018), page 125.

human rights matters. Since the subject of this paper is a Proposal that may be revised extensively, any amendments to the directive made beyond 15 April 2023 will not be considered. The date is chosen partly so the reader will know when the cut-off date applies, but also since any amendments done prior to this date will be manageable in terms of research and analysis.

1.5 Outline

After the introductory Section 1, Section 2 opens with an overview of the background and personal scope to the Proposal together with a definition of what an adverse human rights impact is. The scope of the required due diligence is then studied and problematised in Section 3 so as to contextualise the later Sections. Human rights due diligence soft law is then researched in Section 4, where, *inter alia*, reputational risks as a source of normativity in business and human rights soft law is discussed. Section 5 investigates meaningful stakeholder engagement by way of presenting different methods of engaging stakeholders. This includes presenting some circumstances regarding the case of the Tazreen Fashions garment factory fire to illuminate shortcomings of social audits, which is then juxtaposed with stakeholder consultations. The case of Tazreen Fashions will also provide for discussions of the practical application of the provisions in the Proposal. Both methods (social auditing and stakeholder consultations) are then discussed to highlight strengths and weaknesses in the methods and provide a basis for what meaningful stakeholder engagement ought to entail. Section 6 uses the above-mentioned Sections to facilitate discussions into select provisions in the Proposal related to stakeholder engagement in a broad sense. Finally, the research conclusions will be presented in Section 7, in an order of enumeration that corresponds to the research questions presented in the introductory Section.

2 Proposal for a Corporate Sustainability Due Diligence Directive

2.1 Background to the Proposal

To achieve the UN Sustainability Development Goals, the Commission's position is that extensive systems need to be embedded in companies' processes that aim to mitigate adverse human rights and environmental impacts in large EU-companies' value chains.[22] Large EU Companies rely on global value chains, many times with suppliers in third countries which can make it difficult to identify and mitigate risks of adverse impacts in value chains.[23] Despite some EU companies utilizing voluntary processes and methods of conducting human rights due diligence, the improvements have largely been limited.[24] These problems are compounded by the tendency of global value chains to be ripe with human rights violations, a problem exacerbated by the complexity of global value chains creating large deficiencies in the information that reaches companies that are impacting a community or region.[25] There are also perceived imbalances in the evenness of the playing field for operators in global value chains. One perceived competitive advantage that may benefit companies with the means to deploy voluntary human rights due diligence systems is goodwill and reputational advantages, since investors and consumers are increasingly expecting sustainable development action from companies.[26] Companies that deploy voluntary due diligence, and thereby gain this competitive advantage, are usually large companies.[27] A recurring theme throughout the preamble to the draft documents and other preparatory works to the Proposal is that the impact of voluntary human rights due diligence (*i.e.,* human rights due diligence soft law) is limited.

> "Voluntary measures and initiatives of businesses, trade unions, business organisations and other stakeholders, such as sectoral dialogues and sectoral or thematic multi-stakeholder platforms or initiatives as well as awareness raising amongst consumers, play an important role, but by themselves are unlikely to significantly change the way businesses manage their social, environmental and governance impacts and provide an effective remedy to those affected"[28]

[22] Commission's draft, Explanatory Memorandum, page 1.
[23] Commission's draft, Explanatory Memorandum, page 1.
[24] Commission's draft, Explanatory Memorandum, page 2.
[25] Commission's draft, Explanatory Memorandum, page 1-2.
[26] Commission's draft, Explanatory Memorandum, page 2.
[27] Commission's draft, Explanatory Memorandum, page 2.
[28] European Commission (2020): Study on due diligence requirements through the supply chain; Council of the European Union (2020): Council Conclusions on Human Rights and Decent Work in Global Supply Chains, Recital 21.

There are already countries, some of which are Member States, that have introduced legislation on mandatory human rights due diligence. The scope of these legislative instruments, as well as the required due diligence and methods of enforcement diverge in the countries that have embraced sustainability due diligence. Some Member States are expected to abstain from legislating altogether.[29] Based on the foregoing, the Commission's proposal presumed that the disparities in national legislation may fragment the internal market, and that any fragmentation is likely going to increase.[30] This outcome has been predicted before, where it was theorized that the disparities in sustainable legislation could be expected on account of the right of nations to legislate within their jurisdiction.[31]

A consequence of the fragmentation of domestic EU Member State legislation is the risk of an uneven playing field for the companies that operate in the Union.[32] The unevenness may be the result of large companies that operate globally finding themselves subject to more than one state's sustainability due diligence requirements, ultimately resulting in compliance requirements from two or more jurisdictions which in turn could be mutually incompatible or disproportionately burdensome. Competitive advantages could then be had by operators that don't meet the criteria needed to be subject to any national law of a Member State concerning sustainability due diligence.[33] Moreover, the Commission mentions that a lack of harmony within the Union markets may lead to production and entry and exit of goods and services being more beneficial for companies that either operate in jurisdictions that do not have as extensive sustainability due diligence requirements as the jurisdictions of competitors, or the competitive advantage could stem from companies choosing to operate in such a way so as to avoid heavily regulated jurisdictions.[34]

Having fragmented mandatory human rights due diligence regimes in the Union may also create a race to the bottom in terms of personal and material scope if the legislation is not harmonised or at least aligned with international standards of responsible business conduct.[35] These competitive imbalances as well as the possible obstacles to free movement caused by disparities in national legislation of Member States are sought to be prevented by the harmonisation of obligations on sustainability due diligence. Such harmonisation would benefit cross-border cooperations and investments since the corporate sustainability requirements would be shared and familiar to companies and therefore lower transaction costs.[36]

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[29] Commission's draft, Explanatory Memorandum, page 10- 11, see also footnotes 44, 48-50 to the preamble.

[30] Commission's draft, Explanatory Memorandum, page 11.

[31] Deva & Birchall (2020) page 107.

[32] Commission's draft, Explanatory Memorandum, page 11.

[33] Commission's draft, Explanatory Memorandum, page 11.

[34] Commission's draft, Explanatory Memorandum, page 12.

[35] Commission's draft, Explanatory Memorandum, page 12.

[36] Commission's draft, Explanatory Memorandum, page 11.

2.2 Personal Scope

Article 2 of the Proposal provides the prerequisites for the personal application of the directive on companies in or outside the union ("Company/Companies").[37] The qualifiers are, as were the qualifiers in the Commission's draft, the number of employees and the net global turnover, or net turnover generated within the Union for non-Union Companies.[38] The thresholds for the required number of employees and global turnover have remained unchanged in the Proposal.[39] The Companies subject to the due diligence requirements of the Proposal can be divided into three distinct categories.

Because the directive includes indirect personal scope, there will be other companies in the proximity of any Company subject to these rules that may in some cases be required to take action (*e.g.* business partners that will be required to enter into contractual clauses with a Company, undertaking to adhere to a prevention action plan),[40] but the direct, non-voluntary, categories of in-scope Companies are as follows:

Firstly, Companies formed in accordance with the legislation of a Member State with an average of above 500 employees and a net global turnover of more than EUR 150 M in the last financial year.[41] Second, Companies formed in accordance with the legislation of a Member State with an average of above 250 employees and a net global turnover of more than EUR 40 M.[42] At least EUR 20 M of the global turnover for this second category must have been produced in so called "high-risk", or "high-impact" sectors for the Company to qualify.[43] High-risk and high-impact are used interchangeably.

These sectors include *inter alia* manufacture of clothing, shoes and related products, manufacture of food and beverages and oil, gas and mineral extraction industries.[44] The sectors are based on the OECD Due Diligence Guidance for Responsible Business Conduct ("OECD Guidance") and represent some of the most vulnerable sectors regarding human rights and the environment.[45] For both categories above yet another prerequisite is that they have either produced or should have produced financial statements for the last financial year.[46] Further, the Companies must meet the criteria provided in either the first or second category for two consecutive financial years before they qualify.[47]

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[37] The Council's Proposal, Main Elements of the Compromise, Para 12.
[38] The Council's Proposal, Main Elements of the Compromise, Para 12.
[39] The Council's Proposal, Main Elements of the Compromise, Para 14.
[40] The Council's Proposal, Article 7.
[41] The Council's Proposal, Article 2.1.a.
[42] The Council's Proposal, Article 2.1.b.
[43] The Council's Proposal, Article 2.1.b.
[44] The Council's Proposal, Article 2.1.b.i-iii.
[45] The Council's Proposal, Recital 22.
[46] The Council's Proposal, Article 2.1.a-b.
[47] The Council's Proposal, Article 2.3.a; Recital 21.

The third group of Companies are ones not formed in line with EU Member State law (*i.e.* Companies from third countries) and can in turn be divided into two subsets of groups.[48] These are Companies with a net turnover of more than EUR 150 M in the EU, and Companies with a net turnover of more than EUR 40 M (but less than EUR 150 M) in the EU if EUR 20 M or more was generated in the high-risk sectors enumerated in Article 2.1.b. referred to above.[49]

These non-EU Companies do therefore not need a subsidiary or a branch in the Union in order to be in-scope, rather their economic impact in the Union is a qualifier.[50] Evidently, third country Companies are not assessed on the basis of the average number of employees but only on the turnover in the EU. This is done to fixate on the territorial connection between the third country Company and its operations in the Union, where the net turnover generated represents its potential or actual effect in the Union thereby granting the EU territorial jurisdiction over it.[51]

The decision not to include employees as a qualifier for third country Companies is also based on the fact that "employee" as a term within the scope of the Proposal is based on EU law and could present difficulties in interpretation and application for national supervisory authorities when assessing the standing of third country Company workers.[52] Contrastingly, the Guiding Principles are not limited in scope and instead embeds a corporate responsibility to protect all international human rights, regardless of the size or operational context of the undertaking.[53] The measures needed to satisfy such obligations do however vary depending on the above-mentioned factors as well as *e.g.,* the relevant sector of operations, ownership, and structure.[54]

A business relationship is had with a business partner, which can be in either direct or indirect business with the company.[55] If the business partner has a direct commercial agreement with the company regarding services or product, then it is a direct business partner.[56] An indirect business partner does not have a commercial agreement with the Company, but performs business operations related to the operations of the Company (*e.g.* a manufacturer that delivers products to the Company's supplier, but not directly to the Company).[57]

[48] The Council's Proposal, Article 2.2.
[49] The Council's Proposal, Article 2.2.a-b.
[50] The Council's Proposal, Main Elements of the Compromise, para 13.
[51] The Council's Proposal, Recital 24.
[52] The Council's Proposal, Recital 24.
[53] UNGP, Principle 14.
[54] UNGP, Principle 14.
[55] The Council's Proposal Article 3.e.
[56] The Council's Proposal Article 3.e.i
[57] The Council's Proposal, Article 3.e.i-ii.

2.3 Adverse human rights impact

"Adverse human rights impact" is, pursuant to the Proposal, to be understood as impacts on persons which can be linked to abuse of the human rights listed in Annex I, Part I Section 1 ("Section 1"), which in turn are linked to the instruments enumerated in Annex I, Part I Section 2 ("Section 2").[58] Not all human rights from the instruments mentioned are enumerated in Section 2. To the extent abuse happens as regards a human right embedded in the instruments but which are not enumerated in Section 1, they may still be considered an adverse human rights impact if (i) the human right can be abused by a private entity,[59] (ii) the abuse infringes on one of the interests protected in the instruments enumerated in Section 2,[60] and the company at fault ought to have reasonably identified the abuse based on the circumstances, the extent of its business operations and chains of activities, sectorial, geographical and operational contexts.[61]

Adverse impacts on human rights include, *inter alia*, forced labour, child labour, inadequate workplace health and safety, exploitation of workers, environmental impacts such as greenhouse gas emissions, pollution, and loss of biodiversity.[62] As an example, we can observe the Tazreen Fashions factory fire (see Section 5.2 below) and see whether it constitutes an adverse human rights impact within the meaning of the Proposal. The term "adverse human rights impact" is defined in Article 3.c as either one of the abuses of human rights that are listed in Section 1, or one of the rights in the human rights instruments enumerated in Section 2.[63] In this case, the rights to enjoy just, favourable, safe, and healthy working conditions are embedded in Section 1, para 7 and shall be interpreted in line with Article 7 of the International Covenant on Economic, Social and Cultural Rights.

Article 7.c of the International Covenant on Economic, Social and Cultural Rights provides that States Parties to the Covenant recognize the right of everyone to the enjoyment of just and favourable conditions of work which ensure, in particular safe and healthy working conditions.[64] This right, if violated, constitutes an adverse human rights impact within the meaning of Article 3.c.i of the Proposal, which is always considered an adverse human rights impact without first assessing circumstances. In contrast, if there was another violation of the measures of the International Covenant on Economic, Social and Cultural Rights not included in Section 1, then the circumstances needed to be assessed on a case-by-case basis. An adverse impact is deemed

[58] The Council's Proposal, Article 3.c.i.
[59] The Council's Proposal, Article 3.c.ii, para 1
[60] The Council's Proposal, Article 3.c.ii, para 2
[61] The Council's Proposal, Article 3.c.ii, para 3
[62] Commission's draft, Explanatory Memorandum, page 2.
[63] The Council's Proposal, Article 3.2.i-ii
[64] International Covenant on Economic, Social and Cultural Rights Article 7.c; The Council's Proposal, Annex I, Part 1 Section 1.

to be severe if it is "especially significant" by nature or affects many individuals or is hard to restore once actualised.[65]

[65] The Council's Proposal, Article 3.l.

3 Scope of the Required Due Diligence in the Council's Proposal

3.1 Identifying Adverse Impacts

Where it is relevant, Companies shall carry out stakeholder consultations with groups vulnerable to adverse impacts to gather information on potential or actual adverse impacts. [66] This obligation explicitly covers workers and other relevant stakeholders. The Proposal does not elaborate how the assessment of relevancy is to be made, nor does it offer any elaboration on the contents of such a consultation either, only that conducting it will aid Companies in performing meaningful human rights due diligence and that the targets are both groups of stakeholders and individuals.[67] The Commission will however develop guidelines together with EU agencies, Member States, and non-governmental organisations with the aim of providing companies and authorities in Member States with support on how to fulfil due diligence obligations pursuant to the Proposal. [68] These guidelines will contain sector specific guidance as well as guidance into specific adverse impacts and will be available within two years of the eventual entry into force of the Proposal.[69] Companies will have an obligation to take appropriate measures to identify actual and potential adverse human rights impacts.[70]

This would include the stakeholder consultations mentioned above. The term "appropriate measure" is recurring in the directive and, if performed, entails that a Company is compliant with the material obligations related to carrying out due diligence, regardless of whether it pertains to identifying an adverse impact, preventing it or bringing it to an end.[71] What makes a measure appropriate is whether it is proportionate to the possible severity and likelihood of abuse.[72] The means available to the Company as well as the circumstances in which the potential or actual adverse impact exists (*e.g.,* sector-specific or contract-specific) also plays into what constitutes appropriate measures on the part of the company.

[66] The Council's Proposal Article 6.4.
[67] The Council's Proposal Recital 26a.
[68] The Council's Proposal Article 13.
[69] The Council's Proposal Article 13.
[70] The Council's Proposal Article 6.1.
[71] The Council's Proposal Article 3.q; The Council's Proposal, Recital 29.
[72] The Council's Proposal Article 3.q; The Council's Proposal, Recital 29.

For instance, if a Company cannot receive information pertaining to a potential adverse impact regarding a business partners operations because the partner refuses, and there are no legal methods of forcing them to comply with the demand, it cannot be held against the company.[73] As regards appropriate measures, the obligations laid out in the Proposal are explained to be intended as "obligations of means" meaning that the Companies subject to the provisions of the directive are expected to take the appropriate measures which can reasonably be expected to lead to preventing and mitigating adverse impacts under the circumstances of the specific case.[74] Hence, Companies are not expected to under all circumstance guarantee that adverse impacts will be identified, prevented, and brought to an end.[75]

During the identification process, account should be taken to circumstances that pose risks, such as reports of a business partner being historically prone to abuse human rights, or if there are public records of non-compliance with the national provisions following the Proposal.[76] The identification of potential or actual adverse human rights impacts should be dynamic and regular, at least every 24 months, or upon significant changes to a Company's relationship.[77] A significant change can come in the form of *e.g.* a shift in the dynamics governing a business relationship, changes to the operations of a Company, its subsidiaries or business partners or it could be the result of other substantial changes to conditions regarding *e.g.* law, news about human rights abuses or revealing information received from stakeholders.[78]

Companies that are enumerated in Article 2.1.b and 2.2.b (*i.e.,* Companies in high-impacts sectors) only need to identify adverse impacts relevant to their respective sector.[79] This seemingly limits the scope of the Proposal further, especially to the benefit of Companies active in high-impact sectors that may wish to aim for the bottom of human rights due diligence standards. However, this is not intended by the Union legislator to be an alleviation of the burden to identify adverse impacts, since these sectors have been embedded in the Proposal on the basis of their inclusion in the OECD Guidance.[80] The Proposal refers to the OECD soft law which can be interpreted such that Companies that operate in high-risk sectors can expect to continue using these instruments until the Commission adopts its own guidelines.[81]

[73] The Council's Proposal, Recital 29. The situation described may however lead to an obligation on the part of the Company in question to suspend or terminate the business relationship, see Section 6.3 below.

[74] Council general approach, Recital 15.

[75] Council general approach, Recital 15.

[76] The Council's Proposal, Preamble, Recital 30.

[77] The Council's Proposal, Preamble Recital 30.

[78] The Council's Proposal, Preamble Recital 30.

[79] The Council's Proposal, Article 6.2.

[80] The Council's Proposal, Recital 22.

[81] Compare The Council's Proposal, Recital 22 and The Council's Proposal Article 13.

3.2 Value chains and chains of activities

The terms global supply chains, global value chains and value chains are used interchangeably in this paper, but they generally address somewhat different scopes. Both global value chains and value chains take the upstream and downstream events into account.[82] The Global Value Chain, however, implies an even wider scope since the distance between the worker in the production factory and the end consumer can be vast.[83] The distinction is however inconsequential to the purposes of this thesis and the terms are therefore used interchangeably. The Council left out the use of a product or service from the downstream due diligence required by companies.[84] "Value chain" was instead replaced by "chains of activities", mainly as an appeasement of differing opinions of member states on whether to cover Companies' whole value chains.[85]

This has an impact on the material scope of the due diligence since limiting the scope of the value chains limits the scope of required due diligence. While the Proposal's definition of "chains of activities" has departed with the more sprawling term "value chains", it still covers the activities of downstream business partners, but excludes usage. The choice of a restricted downstream definition of value chains (*i.e.,* excluding usage of a product or service) is however not in line with the common definition used in the OECD Guidelines, the UNGP, or economic supply chain theory. [86] This shift in scope has been described as a disingenuous attempt to redirect human rights due diligence standards by acting as if the standard has never encompassed the whole value chain proper.[87] The Council's explanation for the narrowing of the scope as a result of negotiations between member states is shallow and leaves a lot to be desired in terms of seeing the considerations made.[88] The Commission's draft defined value chains as:

> "[…] activities related to the production of goods or the provision of services by a company, including the development of the product or the service and the use and disposal of the product as well as the related activities of upstream and downstream established business relationships of the company."[89]

[82] Van Dijk & Trienekens (2012), page 13.
[83] Van Dijk & Trienekens (2012), page 13.
[84] The Council's Proposal, Main Elements of the Compromise, para 19.
[85] The Council's Proposal, Article 3.g.; The Council's Proposal, Main Elements of the Compromise, para 18-19.
[86] OECD Watch (2022) "Setting the record straight"; Van Dijk & Trienekens (2012), page 13.
[87] OECD Watch (2022) "Setting the record straight", Accessed 31 March 2023.
[88] The Council's Proposal, Main Elements of the Compromise, para 19.
[89] Commission's draft Article 3.g.

The Council instead opts for a definition which covers essentially the same points but uses the term "chains of activities" to place emphasis on the supply chain, and excludes usage.[90] Further, the new definition is more detailed than the previous, for instance it includes explicit steps in the supply chain that are included in the definition of chains of activities by dividing Article 3.g into two sub-articles that detail the included upstream and downstream activities respectively.[91]

The UNGP Interpretive Guide provides a definition of value chain that is more sprawling in practical terms. Rather than defining the upstream and downstream reach of a chains of activities, the UNGP defines value chains as "activities that convert input into output by adding value" and "includes entities with which it [the company in question] has a direct or indirect business relationship and which either (a) supply products or services that contribute to the enterprise's own products or services, or (b) receive products or services from the enterprise."[92] The risk-based approach developed in the Guiding Principles and the OECD Guidelines entails a flexible approach to the identification of adverse impacts of a business and does not limit the affected areas of interest by differentiating between steps in the value chain.[93]

The division of the value chain into an upstream and downstream system (*e.g.* by calling it "chains of activities" and defining its phases) has been called arbitrary since the concept of value chains is commonly understood as sprawling rather than a segmented tier-based system.[94] Since usage of products or services is not within the scope of the due diligence requirements the directive leaves room for human rights violations in the downstream chains related to the use of products. An example of such possible violations is the hypothetical seller of rubber bullets not having to put into practice the appropriate measures to identify, prevent and mitigate adverse impacts caused by the buyer of the bullets.[95]

The exemption on usage has been called an oversight on the part of the Council that can stifle meaningful improvements on human rights within the union with potentially global consequences to the state of business and human rights law.[96] All in-scope companies must take appropriate measures to identify adverse impacts in their operations or the operations of a subsidiary or a business partner (either direct or indirect business partners) if the business partners operations are relevant to the company's *value chains of activities*.[97]

[90] Council's draft, Main Elements of the Compromise, Recital 18-19.

[91] The Council's Proposal, Article 3.g.i-ii.

[92] UNGP Interpretive Guide page 8.

[93] OECD Watch (2022) "Setting the record straight".

[94] OECD Watch (2022) "Setting the record straight".

[95] Amnesty International (2023), EU: Exemption on the use of products, including tools of torture, from planned EU business human rights law is a dangerous oversight.

[96] Amnesty International (2023), EU: Exemption on the use of products, including tools of torture, from planned EU business human rights law is a dangerous oversight.

[97] The Council's Proposal, Article 6.1.

The term "value chains of activities" seems out of place in the broader context of the Proposal since the term "value chain" was discarded in favour of the term "chains of activities".[98] Value chains of activities is only used once in the Proposal and is not provided with a definition. It raises questions as to the contents of the intended scope since there is no definition of value chain, and the recitals make it clear that the council finds "value chains" materially distinct from "chains of activities". The Council considers "chains of activities" to be a more neutral term, implying that "value chain" is more charged.[99] What values the latter is charged with is not clear. The definition of "Chains of activities" in the Council's draft illustrates that the term is a trade-off between the terms "value chain" and "supply chain", partly because it is a combination of the terms, and partly because it envelops activities both upstream and downstream without covering the traditional value chain.[100]

The identification of adverse impacts thus pertains to an in-scope company's own operations, the operations of its subsidiaries and business partners, the latter only to the extent it is relevant to the Company's value chains of activities.[101] What value chains of activities means is unclear, so identifying actual and potential adverse impacts, a central part of the due diligence process, seems therefore to be lacking in legal clarity.

Mapping of Company's business partners' operations only applies to the extent that the business partner is related to the in-scope company's chains of activities, rather than their value chains of activities.[102] The results of those mappings are later foundational for more in-depth assessments of potential adverse impacts.[103] Companies can therefore be said to have a general duty to take measures to identify adverse impacts in business partner's operations where they are relevant to the Company's "value chains of activities" and a narrower duty to map business partners' operations in the Company's "chains of activities". The Commission's draft contained no provision on mapping, and instead used only Companies' "value chains" to refer to the scope of the required identification of adverse impacts in business partner's operations.[104] This makes the Commission's draft a more accessible piece of legislation, as well as aligned with international standards of responsible business conduct. The term "value chain" is provided a definition in the Commission's draft without injection of other values into the term (*i.e.,* combining terms).

Aside from the uncertainty of the extent of the duty to identify adverse impacts in value chains of activities, the Proposal uses more ambiguous terminology. For instance, the duty to map is something Companies "may" do, and in the preamble to the directive, it is explained that it "should" be done, which

[98] The Council's Proposal, Main Elements of the Compromise, para 18.
[99] The Council's Proposal, Main Elements of the Compromise, para 18.
[100] The Council's Proposal Article 3.g.i-ii.
[101] Council's draft Article 6.1.
[102] Compare The Council's Proposal Article 6.1 and 6.1a.
[103] The Council's Proposal Article 6.1a.
[104] In the Commission's draft, the term "established business relationships" was used instead of "business partners".

can be contrasted with the stronger "shall", present in *e.g.,* the general duty to identify adverse impacts.[105] Such uncertainties may lead Companies to withhold information from the public so as not to create paper trails which can cause them reputational damage, sanctions or civil liability.[106]

3.3 Determining appropriate measures

Companies must take appropriate measures to prevent or mitigate potential adverse impacts that are, or ought to have been, identified.[107] An "appropriate measure" is defined in the CSDDD as a measure sufficient to achieve due diligence proportionate to the level of likelihood of an adverse impact and its potential severity.[108] Appropriateness is determined, in part, by taking into account whether the Company in question is the sole person at fault or if the potential impact was caused together with a subsidiary or business partner, or if it was solely caused by a business partner in the Company's chains of activities.[109] Further, it is relevant to gauge where the potential impact occurred, *i.e.* whether it occurred in a subsidiary's operations or in the operation of a direct or indirect business partner, and also whether the Company had the ability to influence business partners causing the potential adverse impact.[110]

When deciding whether the company has taken appropriate action which can reasonably be expected to result in prevention and mitigation of adverse impacts, the specificities of the particular business operations and chains of activities, sector or geographical area wherein the Company's business partners are operating, the influence the company has over its direct and indirect business partners, and whether the company could increase the power of that influence is taken into account.[111] For instance, the Council draft provides in its preamble that there is an expectation on Companies that they should be able to bring adverse impacts in their own operations or the operations of subsidiaries to an end.[112] When the adverse impact is brought on by a business partner, however, then the standard of expectation is somewhat lower, namely that Companies in scope aim to mitigate the effects of an adverse impact, and the outcome should be as closely aligned to bringing the impact to an end as is possible.[113]

[105] The Council's Proposal, Recital 30.
[106] Deva & Birchall (2020), page 103.
[107] The Council's Proposal Article 7.1.
[108] The Council's Proposal Article 3.q.
[109] The Council's Proposal Article 7.1.a.
[110] The Council's Proposal Article 7.1.b-c.
[111] The Council's Proposal, recital 15.
[112] The Council's Proposal, Recital 38.
[113] The Council's Proposal, Recital 38.

3.4 Discussion

The use of the "chains of activities" and "value chains of activities" regarding the scope of required due diligence in a Company's business partner's operations causes uncertainties, especially since one of the reasons for the Proposal was the emergence of global supply chains and the term "value chain" is an established element of business and human rights law. The general obligation to identify adverse impacts relates to a Company's business partners in the Company's "value chains of activities". As shown above, there is no definition of the term, nor does the amalgamation of the terms "value chains" and "chains of activities" provide for easy interpretation as to what values are left in and which values are not. This is problematic since Companies are meant to assess their value chains of activities when determining how far in the supply chain they must aim to conduct human rights due diligence.

Based on the foregoing and the above investigation we can assert that (i) the scope embedded in *value chains of activities* and *chains of activities* is more limited than traditional value chains, (ii) the term that applies when Companies are assessing their mandatory due diligence requirements is not defined, (iii) this requirement to identify adverse impacts in a business partners operations is more extensive than the duty to conduct mappings (iv) which pertains only to operations of a business partner in a Company's chains of activities.

The mapping is meant to serve as a way for Companies to actively seek out vulnerable nodes in its chains of activities to then investigate in-depth while the general identification process is a catch-all (albeit with limited and ambiguous scope). One argument for the decision to split the identification process into identification and mapping of areas of operations separately could be that, since the obligation to identify adverse impacts pertains to "value chains of activities" and is to be performed by way of stakeholder consultations and quantitative and qualitative information gathered through a number of sources, it gives the due diligence both spread and depth when combined with the mapping of vulnerable areas in the "chains of activities".

Deploying the same effort for both identification and mapping could result in more unfocused, end thereby more shallow, due diligence.

While the above acknowledges that Companies need to engage with stakeholders to a realistic extent and with focused effort, one central aspect of the critique aimed at the Proposal is that the narrowing of the scope prevents the mandatory due diligence to be as encompassing as the soft law it is based on, and this is at the expense of stakeholders in global supply chains and promotion of harmonised international business and human rights practices. The divergence is seemingly drawing a line between what EU Companies should consider materially good scope and what the standard that the rest of the

international business and human rights community is working towards accomplishing.

However, it should be noted that the term "value chains of activities" lacks any accompanying definition and is a novel concept, which is problematic since due diligence in those areas is formulated as an obligation. The issue of whether the scope is as limited as established human rights due diligence is therefore not entirely evident since the comparison is made between a sprawling value chain and a nebulous, undefined, value chains of activities. This lack of clarity is especially troublesome considering that the identification of adverse impacts is the bedrock of any following measures that the Company will take, and without clarity as to the extent of the obligations, it opens for exclusion of nodes in global supply chains that may very well have been within the intended scope of the Proposal.

To add to the confusion presented in the Council's Proposal, the Commission's draft used the term "value chain" and did not break the identification process into two separate sets of obligations, nor was there a variable scope as is used in the Proposal. If the Council had chosen to use one of the supply chain terms used and not separated the identification into two phases, the Proposal may have presented a more cohesive impression. Granted, it would ultimately be a less enveloping scope compared to the Commission's proposed due diligence, but it would be more predictable. The unclarities described are disappointing considering the time and effort that has gone into negotiating the Proposal and the interests behind the move to legislate. The Council's Proposal seemingly misses one of the most central ideas that the UNGP was able to relay, namely that business and human rights isn't exclusively for large companies with resources to comply with high standards, but should be the aim of every business. The chosen form of the process of identifying adverse impacts is ultimately detrimental to the overall impact of the Proposal.

Meaningful stakeholder engagement is obscured because of the ambiguity of the terms used to define the scope of required due diligence. The method of assessing where to engage with stakeholders pursuant to a Company's due diligence obligations is divided into a general requirement and a more in-depth responsibility to probe vulnerable parts of operations. The decision for doing so was not explained by the Council, which shows a lack of attentiveness to the Companies' and public's need for clarity, further exacerbated by the fact that the provision in question is one of the central components to Proposal.

4 Human Rights Due Diligence Soft Law

4.1 Soft Law, Hard Law, and CSR

Soft law is non-binding yet works to shape and influence international law, thereby providing a stepping stone for hard law.[114] Examples of international soft law instruments include standards, guidelines, recommendations, codes of conduct and non-binding resolutions.[115] This can be contrasted with international hard law which is a binding instrument, typically a treaty binding on states or domestic rules applicable to private entities such as companies.[116] The term "soft law" provides for academic contention, as some claim that the phrase has been used to describe such a wide range of legal matters so as to wash it of any practical meaning.[117] Others hold that the phrase demeans the value of binding law and obscures what is law and what is political manoeuvring.[118] Yet another characterisation of soft law is that it lacks enforceability, which is perceived as one of the most useful tools at the disposal of the authority upholding positive law.[119]

Further characteristics of soft law is that it has normative contents that by its origin and material subject and quality provides support for at least parts of whatever provisions it contains.[120] The above could also be summarized as "soft law is authoritative because of its social status and perceived importance". The advantage of soft law in a business and human rights context is perhaps embedded in its non-binding nature. It is faster and simpler to author and adopt soft law since it is derived from a variety of other binding and non-binding instruments and can be more inclusive on account of the lack of enforcement.[121] Moreover, soft law can indeed become binding by way of contractual obligations, thereby solving the enforceability issue.

The relative ease of development and adoption further reduces costs typically associated with the legislative procedure.[122] Hard law, on the other hand is perceived as more concrete since it may require more precision than soft law, and the power of enforcement embedded in the supervising body is, ideally, conducive to system-wide compliance.[123] This is also why hard law may be viewed as more preferential in the sphere of human rights; the enforcement

[114] Cerone, Gammeltoft-Hansen & Lagoutte (2016) page 1.
[115] OECD Regulatory Policy definitions: https://www.oecd.org/gov/regulatory-policy/irc10.htm. Accessed 21 March 2023.
[116] Bosi (2021) Accessed 18 March 2023.
[117] Cerone, Gammeltoft-Hansen & Lagoutte (2016) page 2.
[118] Cerone, Gammeltoft-Hansen & Lagoutte (2016) page 2.
[119] Compare Cerone, Gammeltoft-Hansen & Lagoutte (2016) page 2.
[120] Cerone, Gammeltoft-Hansen & Lagoutte (2016) page 5; page 22.
[121] Boyle (2019) Accessed 26 March 2023.
[122] Bosi (2021) Accessed 18 March 2023.
[123] Compare Bosi (2021) Accessed 18 March 2023.

of non-compliance could be the catalyst for the next leap in the development of business and human rights. A conventional definition of hard law is:

> "[…] legal obligations that are binding on the parties involved and which can be legally enforced before a court."[124]

As mentioned above, soft law can in one sense become hard law when it is legally binding, for instance if it is included in a transaction as responsible business conduct that can entail termination of contract if infringed. When referring to hard law in this paper, the focus is mainly on the mandatory implications applicable to all entities subject to the law in question. While soft law can be enforceable, the inherent voluntarism required for enforcement is what distinguishes hard law from soft law. While instruments such as the UNGP are not mandatory in a legislative sense, many companies do however utilize voluntary measures of self-regulation to promote their sustainability efforts.[125] Deploying a broad understanding of what soft law is in relation to hard law is therefore key in order to have a fuller sense of business and human rights law, since soft law is an amalgamation of many sources of law and no one source in particular.[126]

In the context of international human rights violations, it is possible for a business to be complicit in violations of human rights conducted by States, for instance it could be complicit by forcibly suppressing protests with the help of the military power of an oppressive or authoritarian regime.[127] Such provisions are, however, part of international human rights treaties which address States, meaning that the provisions aimed at states are normally not applicable on private parties. Obligations on companies are instead laid down by the states themselves in domestic legal instruments, and states are also responsible for enforcing the rules.[128]

The boundary between business and human rights soft law and Corporate Social Responsibility ("CSR") is not immediately evident. The Guiding Principles, for instance, are a compilation of obligations and responsibilities related to business and human rights which aim to create a standard of responsible business conduct with both States and companies as its addressees.[129] By way of doing this, the Guiding Principles provide an interplay between international human rights law (both "hard" and "soft"), thereby creating, promoting and reinforcing CSR norms that companies may choose to adopt pursuant to their own interpretations of the soft law.[130]

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[124] ECCHR Glossary, https://www.ecchr.eu/en/glossary/hard-law-soft-law/ Accessed 21 March 2023.

[125] Commission's draft, page 2.

[126] Cerone, Gammeltoft-Hansen & Lagoutte (2016) page 22.

[127] UNGP Frequently Asked Questions, Q 2.

[128] UNGP Frequently Asked Questions, Q 2.

[129] Cerone, Gammeltoft-Hansen & Lagoutte (2016) page 235.

[130] Cerone, Gammeltoft-Hansen & Lagoutte (2016) page 235.

CSR pertains to the voluntary actions of companies based on internal and external pressures to enact on a perceived responsibility related to environmental or philanthropic outcomes rather than profit.[131] The United Nations define CSR as voluntary efforts by companies to improve communities of stakeholders and other philanthropic and environmentally oriented actions.[132] The fundamental difference between CSR and how the Guiding Principles are to be understood is that the Guiding Principles are meant to be implemented on account of an underlying expectation that applies to all companies empowered by the authority of the United Nations, while Corporate Social Responsibility is an exercise in the realization of internal priorities or goals or expectations that a company aims to live up to.[133]

International human rights soft law is often used in international contexts by both international organizations and States.[134] Corporate Social Responsibility is generally understood as a method of management that integrates social aspects into business operations.[135] Since the efforts look the same from an outside perspective, the distinction of CSR and voluntary engagement with human rights due diligence soft law as either externally or internally motivated becomes difficult to gauge, but CSR lacks the harmony and principled foundations of soft law, and CSR also lacks the normativity and political authority embedded in soft law.

4.2 The United Nations Guiding Principles

The UNGP is the business and human rights soft law that provided the starting point for what eventually developed into the standard of responsible business conduct that influenced the Proposal.[136] The UNGP has been likened to a universal language, or "*lingua franca*", in the field of business and human rights law.[137] The UNGP is not enforceable nor binding on private entities and matches the overall profile for soft law discussed above.

Professor John Ruggie[138] presented the Guiding Principles on Business and Human Rights to the United Nations Human Rights Council which unanimously endorsed them in June 2011, establishing the authority of the text.[139]

The three pillars of the principles are (i) duties of states to respect, protect and

[131] United Nations Industrial Development Organization: Corporate Social responsibility.
[132] UNGP Frequently Asked Questions, Q 9.
[133] UNGP Frequently Asked Questions Q 9.
[134] Bosi (2021) Accessed 18 March 2023.
[135] United Nations Industrial Development Organization: Corporate Social responsibility.
[136] Mares (2022)
[137] Bantekas & Stein (2021) page 164.
[138] John Ruggie was a leading figure in developing the UNGP and is regarded as an authority in the area of business and human right.
[139] Bantekas & Stein (2021) page 158; Deva & Birchall (2020) page 63; The Corporate Responsibility to Respect Human Rights, an Interpretive Guide (2012) page 1.

fulfil human rights and fundamental freedoms. The second pillar introduces (ii) a corporate responsibility to respect human rights and the third pillar, which (iii) recognises the need for rights and responsibilities to be matched to appropriate and effective remedies upon infringements.[140]

Unlike the Proposal, the UNGP are applicable to all companies, regardless of size, turnover or other attributes.[141] The Guiding Principles are an attempt to standardise international due diligence norms, which may explain why the UNGP does not limit itself in personal scope.[142] The principles work together to create reference points for states in the nurturing of business and human rights regimes, as well as provide companies with a more profound understanding of the risks of adverse human rights impacts and how they may be managed as well as benchmarking business respect for human rights for the utility of stakeholders and companies that wish to appropriate the principles.[143]

Even prior to the endorsement of the Guiding Principles, the confidence in the framework and its principles appeared to be strong.[144] Former UN High Commissioner for Human Rights stated:

> "These Guiding Principles clarify the human rights responsibilities of business. They seek to provide the first global standard for preventing and addressing the risk of adverse human rights impact linked to business activities. If endorsed, the Guiding Principles will constitute an authoritative normative platform which will also provide guidance regarding legal and policy measures that, in compliance with their existing human rights obligations, States can put in place to ensure corporate respect for human rights."[145]

The impetus for the Guiding Principles was, in part, the emergence of global supply chains.[146]

While global supply chains provide job opportunities, a growing ground for economic cooperation and transfers in knowledge and technology between states, the intention behind transitions from national to global supply chains is often lowering production costs and production time, many times at the expense of workers' labour conditions.[147]

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[140] UNGP General Principles; Bantekas & Stein (2021) page 159; The Corporate Responsibility to Respect Human Rights, an Interpretive Guide (2012) page 1.

[141] UNGP General Principles.

[142] Compare UNGP General Principles.

[143] The Corporate Responsibility to Respect Human Rights, an Interpretive Guide (2012) page 2.

[144] The Corporate Responsibility to Respect Human Rights, an Interpretive Guide (2012) page 2.

[145] Statement by Ms. Navi Pillay United Nations High Commissioner for Human Rights to the Employers' Group at the International Labour Conference (2011), page 5.

[146] Deva & Birchall, page 108.

[147] Deva & Birchall, page 108.

Some organisations even go so far as to assert that some value chains are intentionally being designed to make it hard to discern connections, further obscuring the road to remediation for the victims and accountability for the responsible.[148] The interconnection of global companies also exacerbates the issues of identifying and monitoring human rights and environmental matters since global value chains have many direct and indirect domestic and transnational relationships, making it hard to focus efforts.[149] The human rights due diligence measures of the Guiding Principles have, for some time, been regarded as the primary method by which these global value chain issues may be addressed.[150] John Ruggie's mandate as Special Representative of the Secretary General on the Issue of Human Rights and Transnational Corporations and other Business Enterprises ("SRSG") entailed extensive investigation of practical application of business and human rights and where it harmonises with academic interpretations of the subject.[151]

Stakeholders, including state bodies, national and international human rights institutions, business enterprises on domestic and international level, academics and civil society were consulted.[152] These participants are common as regards stakeholder consultations, but the inclusion of private business enterprises in the consultation rounds was a novel idea.[153] These consultations with the private sector became a central part of the method on which Ruggie based his work.[154] The inclusion of a wide range of stakeholders helped spread the central themes and ideas of the Guiding Principles even before they were endorsed, and further aided the strategic development of the final documents.[155]

Critique of the Guiding Principles includes that there is a risk of creating a false belief that the obligation to respect human rights can be fulfilled by merely setting up and implementing due diligence processes in a company's management systems, which would be detrimental for meaningful compliance since *implementation* does not equate to *compliance*.[156] The former could be performed as a one-off event while the latter requires ongoing monitoring.[157] The essence of the criticism could therefore be said to lie in the risk of creating a corporate climate which genuinely champions human rights due diligence but does not provide the instruments necessary for meaningful compliance (*e.g.,* through compliance-verification and enforcement).

Furthermore, voluntary business and human rights as a concept could be construed as providing companies a venue for green-washing measures and using the veil of voluntarism to explain away actual human rights violations that may occur in their value chains as a symptom of transition and adaptation that can be expected by a company employing voluntary measures.[158]

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[148] European coalition for corporate justice "Our Priorities", Link: https://corporatejustice.org/priorities/ Accessed 16 March 2023.

[149] Deva & Birchall, page 108.

[150] Deva & Birchall, page 109.

[151] Cerone, Gammeltoft-Hansen & Lagoutte (2016) page 244.

[152] Cerone, Gammeltoft-Hansen & Lagoutte (2016) page 244.

[153] Cerone, Gammeltoft-Hansen & Lagoutte (2016) page 245.

[154] Cerone, Gammeltoft-Hansen & Lagoutte (2016) page 245.

[155] Cerone, Gammeltoft-Hansen & Lagoutte (2016) page 245.

[156] Murray & Long (2022), page. 21.

[157] Murray & Long (2022), page 21.

[158] Bantekas & Stein (2021), page 165.

4.3 Mandatory human rights soft law?

John Ruggie's reflections on the voluntary nature of human rights soft law (specifically the UN Draft Norms) during his mandate as SRSG has been criticised.[159] Ruggie stated, *inter alia*, that corporations lack legal obligations *vis-à-vis* business and human rights and that they derive their responsibilities from societal expectations rather than human rights law.[160] David Bilchitz argues that the failure to engage with the moral foundations of human rights leads the SRSG to make several mistakes".[161]

Bilchitz focuses on a distinction between *binding normativity i.e.,* what is lawfully demanded of companies, and *moral normativity i.e.* what ought to be within the sphere of corporate obligation.[162] The essence of the critique is a perceived lack of engagement in the question of the importance of moral normativity on the part of Ruggie.[163] The Interim Report of the Special Representative of the Secretary-General on the issue of human rights and transnational corporations and other business enterprises was the first report by the SRSG in 2006 and had the purpose to "frame the overall context encompassing the mandate as the Special Representative of the Secretary-General sees it, to outline the general strategic approach taken, and to summarize the current and planned programme of activities."[164]

In the Interim report, the SRSG drew conclusions on the binding nature of the UN Draft Norms. Ruggie concluded that, since there are no rules in international law that create obligations for companies (save for some war crimes and crimes against humanity), then there are no non-voluntary obligations for corporations to adhere to the UN Draft Norms.[165] The responsibility for companies to respect human rights is, according to the SRSG, a sentiment that had grown in momentum and was reinforced in close to all soft law instruments, and with the unanimous endorsement of the Guiding Principles by the Human Rights Council gained even further validation.[166]

[159] Deva & Bilchitz (2013), page 107.
[160] Deva & Bilchitz (2013), page 107.
[161] Deva & Bilchitz (2013), page 107.
[162] Deva & Bilchitz (2013), page 109.
[163] Deva & Bilchitz (2013), page 109 ff.
[164] Interim report of the Special Representative of the Secretary-General on the issue of human rights and transnational corporations and other business enterprises (2006), page 1; para 6.
[165] Compare Interim report of the Special Representative of the Secretary-General on the issue of human rights and transnational corporations and other business enterprises (2006), para 60.
[166] "The UN "Protect, Respect and Remedy" Framework for Business and Human Right" (September 2010); Deva & Bilchitz (2013), page 138.

Furthermore, the supervision has been predominantly carried out by non-governmental organisations, companies, and trade unions.[167] Ruggie held that reliance on private supervision entails limitations to the possibilities for success of enforcement efforts unless the public has an influence in the authority of the governance of that private enforcement.[168] A discussion on these limitations will be carried out below in more detail in relation to the National Contact Points of the OECD. As briefly touched upon above, the UNGP is not something that states can ratify and thereby make the principles binding in the same way that a treaty or domestic legislation can become binding. They do however provide a practical application of human rights, some of which are legally binding on states.[169]

The grievance mechanisms and remedies for victims of human rights violations must therefore be provided for by states, since they have the authority to legislate and enforce these rights.[170] Moreover, the responsibility for companies to respect human rights is not the same as an obligation to do so.[171] The Guiding Principles' choice of the term "responsibilities" over the more categoric "obligations" can be construed as further signalling that the Guiding Principles operate on societal expectations, but also draws attention to the need for adherence and market willingness to make the Guiding Principles work. The authority of the Guiding Principles reinforces those responsibilities. Regarding the necessity for hard law on the area, the United Nations Working Group on Business and Human Rights acknowledges that mandatory human rights due diligence instruments like the Proposal are "critical" for the scaling of human rights in business contexts.[172]

In recent years, and especially in relation to the Proposal, the term mandatory human rights due diligence has become common when discussing due diligence provisions that will apply to companies on an enforceable basis, seemingly driving a wedge between voluntary human rights due diligence ("HRDD") (*e.g.* the UNGP) and mandatory human rights due diligence ("mHRDD") (*e.g.* the Proposal).[173] Placing too much emphasis on such distinctions may however be oversimplifying the mechanisms that constitute the normative power of authoritative soft law such as the UNGP and the OECD Guidelines. Moreover, it is not helpful in the process of attempting to identify other sources of normativity that drive business and human rights.

In 2014, the official document titled "Frequently Asked Questions about the Guiding Principles on Business and Human Rights" was published, wherein the by then three-year-old set of principles was elaborated on by the Office of the United Nations High Commissioner for Human Rights ("OHCHR").[174]

[167] Deva & Bilchitz (2013), page 138.
[168] Mares (2011) page 11-12.
[169] UNGP Frequently Asked Questions Q 6.
[170] Compare UNGP Frequently Asked Questions Q 11.
[171] Cerone, Gammeltoft-Hansen & Lagoutte (2016) page 246.
[172] OHCHR: "Mandatory human rights due diligence".
[173] OHCHR: "Mandatory human rights due diligence".
[174] UNGP Frequently Asked Questions.

Regarding whether the Guiding Principles are voluntary, the OHCHR engaged the reader with a categorical "No.", which was then followed by four paragraphs of reservations.[175]

The first addition made to the statement is that States do indeed have an obligation to protect human rights against companies' operations. This obligation on States to protect human rights is derived from international human rights treaties and in that context the Guiding Principles are indeed mandatory.[176] The second reservation is that companies have a duty to adhere to their domestic law which may, to varying degrees, conform to the standards of the Guiding Principles.[177]

Further, the Guiding Principles formulates the risk of causing or being complicit in human rights violations as compliance issues. [178] This could be brought into effect by using contractual mitigation clauses. The fact that contractual clauses can be enforced in a court of law or by way of arbitration is, according to the document, also part of what makes the Guiding principles mandatory.[179] This makes sense considering soft law instruments can be given legal effect by way of voluntary commercial agreements such as compliance undertakings and adherence to principles.

The last argument presented for the Guiding Principles being mandatory is that companies which do not know and show that they respect human rights run the risk of bad will in the "court of public opinion". [180] The reasons presented above were not framed as arguments that by themselves make the Guiding Principles non-voluntary, but rather that they work together to produce a normative effect based on different sources of normative drivers (reputational risk, financial, legal etc.).[181]

To illustrate the variety of norms and mechanisms that are included in the normative scope of soft law, we will briefly discuss reputational risk in the next sub-section.

[175] UNGP Frequently Asked Questions Q 7.
[176] UNGP Frequently Asked Questions Q 7.
[177] UNGP Frequently Asked Questions Q 7.
[178] UNGP Frequently Asked Questions Q 7.
[179] UNGP Frequently Asked Questions Q 7.
[180] UNGP Frequently Asked Questions Q 7.
[181] UNGP Frequently Asked Questions Q 7.

4.4 Reputational risk as a compliance incentive

One particularly complex and hard-to-quantify driver for a need of compliance in economic supply chain theory is indeed the "reputational risk" mentioned in the OHCHR's Frequently Asked Questions discussed above.[182]

The reputational risk system entails that reprehensible behaviour, an "unacceptable act", draws public attention to a company's supply chain which potentially disrupts the company's operations.[183] For instance, an unacceptable act can lead to negative media coverage which prompts Public Relations-activities from the responsible company, costing it time and money.[184] It also means that the reputation of the company is tarnished which leads to more media coverage and at worst a negative feedback-loop that produces more media coverage and reputational damage.[185] Media coverage also leads to issue awareness, which could exacerbate a negative media coverage loop, since the company's actions may become synonymous with the issue that has come to light, even though the problem at its roots is systemic.[186]

The reputational damage can lead to other negative financial effects on the company since access to opportunities may drain on account of other companies not wanting association with the issue awareness raised by the unacceptable act or guilt by association. [187] Naturally, this could entail a negative impact on the sales or overall economic status of the offending company.[188] The negative effects of the reputational risk system as described are a *consequence* rather than an independent *source* of risk.[189] Risk management is therefore more meaningful than damage control for the avoidance of the costs associated with the scenario mentioned above, since the former aims to anticipate and prevent the consequences, while the latter aims to control and minimise damage.[190] The expected savings on time and money which are worked into contracts with global supply chains, *e.g.,* factories, leads to issues such as excessive overtime and worker safety violations.[191]

Unacceptable acts in global supply chains could therefore be a consequence of highly competitive industries pressing margins as low as possible, neglecting health and safety, unsustainable labour recruitment focused on racing the wages to the bottom etc.

[182] UNGP Frequently Asked Questions Q 7.
[183] Elms & Low (2013), page 202.
[184] Elms & Low (2013), Compare Figure 8.5, page 203.
[185] Compare Elms & Low (2013), Compare Figure 8.5, page 203.
[186] Compare Elms & Low (2013), Compare Figure 8.5, page 203.
[187] Compare Elms & Low (2013), page 202.
[188] Compare Elms & Low (2013), Compare Figure 8.5, page 203.
[189] Compare Elms & Low (2013), page 202.
[190] Elms & Low (2013), page 203.
[191] Elms & Low (2013), page 216.

Big brands and other suppliers who source their products from factories operating in poor conditions have been called to take voluntary leadership, but regulation is ultimately perceived to be the likely answer to the discussed risks in global value chains.[192]

4.5 OECD's National Contact Points

The Organisation for Economic Cooperation and Development ("OECD") is an intergovernmental organization that works toward the promotion of social and economic development.[193] The OECD Guidelines are standards and guidance for responsible business conduct which are non-binding on companies.[194] The Guidelines are a set of soft law tools aimed at companies with operations in states that are members to the OECD.[195]

The role of the OECD Guidelines has been phrased by the OECD itself as "non-binding guidance for responsible business conduct in a global context"[196] The Guidelines are detailed and provide for recommendations such as business enterprises being recommended to seek mitigation and prevention of adverse impacts on human rights and have policy commitments in place to respect human rights etc.[197]

The relationship between the OECD Guidelines and the Guiding Principles is evident in the terminology of the Guidelines itself, and the foreword to the OECD Guidelines provides that changes made to them, which were adopted 25 May 2011, include a new chapter on Human rights, consistent with the Guiding Principles.[198] Further, the OECD Guidelines provides commentary, and in the commentary to the Human Rights Section it is explicitly stated:

> "This chapter opens with a chapeau that sets out the framework for the specific recommendations concerning enterprises' respect for human rights. It draws upon the United Nations Framework for Business and Human Rights 'Protect, Respect and Remedy' and is in line with the Guiding Principles for its Implementation."[199]

The enforcement of the OECD Guidelines comes from the National Contact Points ("NCPs"), which are set up by the nations committed to the Guidelines.[200]

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[192] Elms & Low (2013), page 216.

[193] Michalowski (2013), page 37.

[194] Bantekas & Stein (2021), page 207.

[195] Michalowski (2013), page 37.

[196] OECD (2018) Structures and Procedures of National Contact Points for the OECD Guidelines for Multinational Enterprises, page 9.

[197] OECD Guidelines (n. 49) Section IV, para 3; para 4; Bantekas & Stein (2021), page 209 f.

[198] OECD Guidelines, Foreword, page 3.

[199] OECD Guidelines, Section IV, Commentary para 36.

[200] Bantekas & Stein (2021), page 211.

One shortcoming of NCPs is that they lack the authority to sanction non-compliance. They instead function as a mediation instrument for bargaining, persuasion, and compromise among diverse stakeholder groups.[201] The final responsibility of adherence to the guidelines therefore falls within the authority and responsibility of companies.

If a human rights violation would occur in the context of the OECD, then the NCPs would, in most cases, receive a complaint from *e.g.,* a trade union aimed against the offending company. [202] The complaint would then be moved into mediation by the NCP if it deemed the complaint valid. [203] If the mediation does not result in an agreement, then the NCP issues a public statement on the issue.[204] The statements contain information as to the background of the complaint, the opinions of the parties involved, the measures taken by the NCP and what recommendations it has prescribed.[205] A negative statement is purported to sometimes motivate parties to mediate to resolve their dispute.[206]

The operative processes of NCPs are not explained in detail in the Guidelines, and the countries which are signatory to the OECD have varying degrees of success in mediations.[207] Some suggest that the enforcement is procedurally weak because the NCPs are not sufficiently empowered by the OECD Guidelines.[208] The success rate of mediations vary depending on *e.g.,* resources made available to NCPs by their host nation, whether they receive political support and institutionalization. [209] The output of the mediations is less than optimal; only one out of every eight complaints result in a compromise that all parties find agreeable.[210] One hypothesis raised regarding the lack of positive results from the work flowing out of OECD's NCPs is the lack of enforcement power.[211] Large numbers of complaints remain unresolved because companies refuse to engage or cooperate in dispute settlements.[212]

The NCP mediations may also be construed as being politicized since the governments need to embed the NCP in some governmental body's department, and the most well suited are likely commercial departments. For instance, the NCP of the United Kingdom is hosted by the Department for international Trade.[213] Naturally, there could be differences between the level of biases within NCPs between countries based on how they are structured and where they are hosted.

[201] Bantekas & Stein (2021), page 211.
[202] Bantekas & Stein (2021), page 211.
[203] Bantekas & Stein (2021), page 211.
[204] Bantekas & Stein (2021), page 211.
[205] Michalowski (2013) page 38.
[206] Michalowski (2013) page 38.
[207] Bantekas & Stein (2021), page 212.
[208] Michalowski (2013) page 37–38.
[209] Bantekas & Stein (2021), page 212.
[210] Bantekas & Stein (2021), page 212.
[211] Bantekas & Stein (2021), page 212.
[212] Bantekas & Stein (2021), page 212.
[213] Bantekas & Stein (2021), page 213.

In addition to the OECD Guidelines mentioned above, the OECD Guidance provides detailed practical support to enterprises implementing the OECD Guidelines by way of "plain language explanations" of recommendations on due diligence and associated provisions.[214] The OECD Guidance aims to promote a shared understanding of due diligence for responsible business conduct. It also helps any company that aims to implement the UNGP and other soft law instruments such as the ILO Tripartite Declaration of Principles Concerning Multinational Enterprises and Social Policy, since it is essentially, just like the OECD Guidelines, existing standards and policies repackaged in a practical form.[215] The OECD provides for additional detailed guidance instruments to help businesses in specific sectors conduct responsible business, such as in the industries of mineral extraction, manufacturing of garment and footwear, finance and agriculture.[216] Since the OECD Guidelines receive adherence from governments while companies can merely endorse or appropriate the Guidelines but not be signatory to them, other tools can be construed as being more proactive.[217] For instance, the UN Global Compact is a voluntary instrument that companies can join on the basis of adhering to a set of principles thereby becoming signatories.[218] This does however not seem to resolve the problem of enforceability since the voluntary act of becoming signatory to the principles still requires, of course, voluntarism.

In summary, the OECD instruments are authoritative derivatives of the UNGP that aim to promote social and economic growth under the umbrella of the OECD. The National Contact Points are mediation mechanisms that provide venues for dispute resolution but are made suboptimal by the ineffective implementation of their procedures. There are also political issues in the way of effective and harmonised enforcement by the NCPs since their independence may vary based on their institutionalization. They are occasionally successful since they can produce meaningful mediations, but the lack of enforcement power ultimately makes participation on the part of companies a matter of personal discretion.

4.6 Discussion

Soft law such as the UNGP do not derive their normative power from one source of law but rather combines many aspects of both law, social and economic aspects of business to promote a normative narrative. As an illustrative example, we can observe the mechanisms of the reputational risk system described above. The negative media attention that can be created because of a company's reprehensible actions can cause income loss. The reputational risk system is not joined to any specific legal instrument and operates instead on consumer/societal expectations related to moral values.

[214] OECD Guidance, Foreword, page 3.
[215] OECD Guidance, Foreword, page 3.
[216] OECD Guidance, Foreword, page 3.
[217] Bantekas & Stein (2021), page 214.
[218] Bantekas & Stein (2021), page 201; 214.

Other instruments such as the OECD Guidelines can provide for what can be perceived as a middle road between soft and hard law by creating institutions that work as private enforcement on companies (*e.g.,* NCPs).

If a complaint is lodged by a stakeholder such as a trade union, then the NCP would lead the mediations and invite companies to participate, and if their efforts are fruitless then the NCP issues a public statement (which is effectively naming and shaming). The above combined with the empirical inefficiency of NCPs to produce satisfactory outcome of mediations (because of companies' refusal to participate, for instance) makes the mixture of moral, economic, and other normative sources what drives companies to submit to the mediations of the NCPs. And considering that only one eight of mediations produce favourable outcomes, meaning that there were seven companies willing to risk negative attention, indicates that this mixture of societal expectation is insufficient to drive companies to work more proactively with their sustainability matters, despite exposure to *e.g.,* reputational risk.

Voluntary mechanisms of enforcement of business and human rights law through *e.g.,* mediation or naming and shaming are not enough to create a system that effectively promotes meaningful compliance with business and human rights regimes. Other instruments have been said to be more proactive, such as the UN Global Compact, but these are ultimately voluntary as well since there is no external enforcement; enforcement only comes into play once a company has decided to engage with such initiatives.

The lack of enforceability creates a system-wide deficiency in compliance incentives. In this environment, hard law is essential to reach the next step in the development of business and human rights.

5 Meaningful stakeholder engagement

5.1 Contextualising stakeholder engagement

In the context of this paper, stakeholder engagement refers to any actions of a Company that influences or directs the actions, culture, or processes of a business partner. In this sense, stakeholder engagement is not exclusively referring to auditing and consultations as elaborated below, but any interaction with a business partner that is not solely performed on account of commercial considerations. Stakeholder engagement could therefore mean educating stakeholders on their rights, inviting a business partner's management to workshops, as well as ending a business relationship because of lack of adherence to a Code of Conduct.

It may seem unintuitive to consider termination of business relationships as engaging with stakeholders since the relationship is being undone. It is however important to recognize that avoidant behaviour is also action, especially in global value chains where it would be easy for vulnerable stakeholders to be exploited and then abandoned when potentially adverse impacts are brought to light. *Meaningful* stakeholder engagement, however, refers to any engagement that promotes the well-being and visibility of the vulnerable stakeholders in a Company's operations or the operations of its business partner (whether direct or indirect partner). The following Section details some methods of stakeholder engagement.

5.2 Social auditing

Social auditing refers to the process of verifying a business partner's compliance with, typically, a code of conduct ("CoC").[219] Social auditing is included in several soft law instruments as a tool for identifying human rights impacts, but is only one of many potential methods.[220] Other methods are benchmarks, ratings, stakeholder engagement, tracking and responding appropriately to political developments in the supply chains, as well as tracking and analysing the overall output of the relevant industries and having effective grievance mechanisms.[221] Despite these abovementioned measures that can be taken, there are concerns that companies continue to be overly reliant on social auditing.[222]

[219] Deva & Birchall (2020), page 119.
[220] Deva & Birchall (2020), page 119; OECD Apparel Guidance page 27.
[221] Deva & Birchall (2020), page 119.
[222] Deva & Birchall (2020), page 119.

The Worker-driven Social Responsibility Network (WSRN) was created in 2015 with the intention of disseminating, promoting, and duplicating the model of practice in supply chains across the globe. Founding partners were, inter alia, Business & Human Rights Resource Centre, Workers Rights Consortium, Fair Food Standards Council, Migrant Justice etc.[223] The WSRN's position on CSR is that it is a tool for companies to handle their public relations through the adoption of policies pertaining to human rights, without embedding tools of enforcement in their operating processes.[224]

The identification of an adverse human rights impact in the context of CSR is, according to WSRN, a signal for companies to initiate processes to control damage to reputation, rather than a signal that their operations are causing or aiding in the abuse of human rights.[225] The failure of CSR according to WSRN is that it does not place the workers at the centre of the measures taken in order to respect human rights. WSRN holds that, since the workers (*i.e.*, stakeholders vulnerable to a Company's operations) are not part of the development and execution of problem-solving measures, despite being one of the most valuable stakeholder profiles in assessing on-the-ground problems, then CSR as a model for responsible business becomes vapid.[226]

The model endorsed by WSRN is Worker-Driven Social Responsibility (WSR) and is based on the idea that meaningful compliance with human rights can be achieved if the measures are focused on workers, enforcement measures, and legally binding commitments on the part of the corporate top regarding the improvement of working conditions.[227] There are some key distinguishing features of WSR that separates it from CSR, one of which being that enforcement and monitoring procedures are designed to ensure that workers can make themselves heard and be an actual part of their own protection, *e.g.,* by way of being educated on company policies or codes of conduct so they are equipped to identify when misconduct is taking place.[228]

Further, WSR sets out to legally bind large brands and companies to agreements with worker organisations to ensure that the suppliers chosen by the brand will be financially aided to meet wage and working condition designed with the aid and force of worker organisations.[229] The WSRN aims to move away from hands-off approaches such as social audits and move into more stakeholder-centric human rights regimes.

One illuminating example of a failed social audit is the Tazreen Fashions garment factory fire. Walmart Inc. had between 2011 and 2012 conducted several audits of the Tazreen Fashions apparel factory in Bangladesh.[230]

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[223] WSRN: About us, Link: www.wsr-network.org/about-us/ Accessed 29 March 2023.
[224] What is worker-driven social responsibility (WSR)?,page 1.
[225] What is worker-driven social responsibility (WSR)?, page 2.
[226] What is worker-driven social responsibility (WSR)?, page 1.
[227] What is worker-driven social responsibility (WSR)?, page 2.
[228] What is worker-driven social responsibility (WSR)?, page 2.
[229]What is worker-driven social responsibility (WSR)?, page 2.
[230] WSRN Case Study: Tazreen Fashions (Bangladesh).

During at least one of these visits the factory had received an "orange" rating meaning that there were high perceived risks due to poor conditions on site. These were, *inter alia*, blocked escape routes, faulty electrical wiring, insufficient amount and impact of fire extinguishers and a lack of fire alarms.[231] Some reports also claim that the construction of the building was not up to local code.[232]

Walmart is reported to have asked Tazreen Fashions to draw up an action plan which would be presented to the auditor six months later.[233] Walmart instead decided to remove Tazreen Fashions from its list of approved factories, meaning that suppliers would be denied contracts for products produced in Tazreen Fashions' factory.[234] It is not clear why Walmart instead decided to remove Tazreen Fashions from their list of authorized factories.[235]

On 24 November 2012 on the factory ground floor, a short circuit is suspected to have caused flammable materials to ignite, spreading a fire upwards through the floors killing 112 workers.[236] In the aftermath of the disaster, it was discovered that Walmart had suppliers that had sourcing contracts with Tazreen Fashions despite the removal of Tazreen Fashions from the list of approved production plants. This was, according to Walmart, unauthorized subcontracting in breach of Walmart policies (the implication partly being that Walmart had no connection to Tazreen Fashions and could therefore not be accused of any negligence related to the factory fire), yet documentation was found on site indicating that at least three of Walmart's suppliers had subcontracted work to Tazreen after Walmart removed them from the list of authorized factories.[237]

The WSRN laments Walmart, pointing to the historical prevalence of fatal lack of fire safety or structural integrity in the plants of Bangladesh, and that Walmart had acknowledged at a multi-stakeholder meeting in Dhaka prior to the incident that repairs and renovations of Bangladeshi plants were needed on a large scale, but had stated that "It is not financially feasible for the brands to make such investments."[238] Less than a year after the Tazreen Fashions incident, the Rana Plaza collapsed.

The building hosted five garment factories and cost 1,134 worker's lives, making it one of the worst industrial disasters in history.[239] Two factories housed in the Rana Plaza had passed social audits mere months before the

[231] WSRN Case Study: Tazreen Fashions (Bangladesh).

[232] Fatal Fashion: Analysis of recent factory fires in Pakistan and Bangladesh: a call to protect and respect garment workers' lives, SOMO & SCC (2013), page 41.

[233] Fatal Fashion: Analysis of recent factory fires in Pakistan and Bangladesh: a call to protect and respect garment workers' lives, SOMO & SCC (2013), page 40.

[234] WSRN Case Study: Tazreen Fashions (Bangladesh).

[235] Fatal Fashion: Analysis of recent factory fires in Pakistan and Bangladesh: a call to protect and respect garment workers' lives, SOMO & SCC (2013), page 40.

[236] WSRN Case Study: Tazreen Fashions (Bangladesh).

[237] WSRN Case Study: Tazreen Fashions (Bangladesh).

[238] WSRN Case Study: Tazreen Fashions (Bangladesh).

[239] Prentice & Neve (2017) page 45; However, Deva & Birchall (2020) claim that 1,139 people lost their lives, see page 140.

collapse, further indicating that social auditing is limited in its ability to produce meaningful identification of potential adverse impacts.[240]

Social auditing seemingly does not provide for a deep understanding of issues it attempts to asses, nor does it promote effective remediation, and the outcomes are purported to be superficial and short-term.[241] In cases where social auditing manages to identify adverse impacts, there may be structural barriers to meaningful remediation, and the method sometimes fails to identify adverse impacts that ought to have been recognized.[242] The incidents mentioned have not sparked initiatives from the companies and industries at fault, which shows that long term and sustainable considerations are being disregarded in favour of short term benefit.[243] Workers in the industry are still working in unsafe conditions.[244]

The above indicates that, although social audits can provide for positive identification of adverse impacts, it does not seem to produce a sufficiently clear picture of the problem nor the possible solutions, and it sometimes fails to identify adverse impacts altogether. There are, as mentioned above, alternatives to social auditing which may provide a way to supplement social auditing and engage the stakeholders even further.

5.3 Stakeholder consultations

The Proposal came about partly because of poor respect for the human rights of stakeholders in global value chains.[245] Pursuant to the OECD Guidance, stakeholders can be persons or groups whose interests are or may become impacted by the activities of a company.[246] Since the term encompasses many potential stakeholders, the OECD Guidance highlights "relevant stakeholders" as those relevant to a specific activity.[247] The stakeholder collective can further be divided into two subsets of groups namely "stakeholders" in general, and "rightsholders". The latter refers to individuals who are or may have their human rights affected, while the former is a broader term that encompasses *e.g.,* indigenous people's collective rights.[248]

The UNGP defines stakeholders as any individual who is or may be affected by the activities of a company, and an affected stakeholder refers to individuals who have had their human rights affected.[249] The Proposal came about

[240] Deva & Birchall (2020), page 120.
[241] Deva & Birchall (2020), page 121.
[242] Deva & Birchall (2020), page 121.
[243] Deva & Birchall (2020), page 140.
[244] Deva & Birchall (2020), page 141.
[245] Council's draft, Recital 13.
[246] OECD Due Diligence Guidance 2018, Q8.
[247] OECD Due Diligence Guidance 2018, Q8.
[248] OECD Due Diligence Guidance 2018, Q8.
[249] UNGP Interpretive Guide, page 8.

partly because of poor respect for the human rights of stakeholders in global value chains.[250] The definition of stakeholder is important since it can give rise to rights and may be crucial in the discovery of potential adverse impacts since any limitation on the inclusivity of stakeholder profiles entails a limit on the reach of stakeholder consultations.[251]

> "'stakeholders' means the company's employees, the employees of its subsidiaries, trade unions and workers' representatives, consumers, and other individuals, groups, communities, or entities whose rights or interests are or could be affected by the products, services and operations of that company, its subsidiaries and its business partners, including civil society organisations, national human rights and environmental institutions, and human rights and environmental defenders;"[252]

A "possibly affected individual" as described in the article quoted above is poorly elaborated on in the recitals where they are broadly exemplified as human rights or environmental defenders, indigenous peoples that receive protection under the UN Declaration on the Rights of Indigenous Peoples and civil society organisations.[253] The elaboration is thin and places focus on institutional stakeholders such as workers' groups and organisations rather than individual natural persons.

The definition does however frame stakeholders as "[…] other *individuals*, groups, communities or entities whose rights or interests are or could be affected […]"[254] which envelops essentially anyone and gives the term generous scope. It would include *e.g.,* employees of the company, its subsidiaries, and the employees of direct and indirect business partners in the relevant chains of activities. This is in line with the common notion that workers in general are a particularly vulnerable stakeholder profile in global value chains. Below is a presentation of stakeholder engagement as represented in prominent soft law instruments.

5.3.1 United Nations Guiding Principles

Stakeholder engagement in the UNGP Interpretive Guide aims to make visible the people vulnerable to business operations and promotes action

[250] Council's draft, Recital 13.
[251] Compare The Council's Proposal article 6.4.
[252] The Council's Proposal Article 3.n.
[253] The Council's Proposal Recital 26a.
[254] The Council's Proposal Article 3.n. Emphasis added.

reflective of the dignity inherent to every human within those operations.[255] The key to human rights due diligence is the understanding of potentially affected peoples' and individuals' perspectives.[256] If possible and appropriate, the company should therefore consult those who may be affected directly, and if that is neither appropriate nor possible, then their legitimate representatives should be consulted.[257] The more impactful a business' operations are, the more in tune should they be with their affected stakeholders.[258] The engagement of these stakeholders will lead to insight into concerns and fears, and may uncover issues that may become relevant in later stages of operations.

Engaging stakeholders also builds trust and report since it shows that the company values their health, dignity and human rights.[259] One benefit of stakeholder engagement for companies is that disputes may be uncovered before they are actualised, thereby avoiding conflicts with stakeholders.[260]

Since human rights due diligence relates to the core operations of a business, it is ill-advised to perform stakeholder engagement solely through third parties.[261] An instrument of due diligence related to stakeholder engagement is social auditing, wherein an auditor is sent to inspect compliance with ethical codes. In those cases, it may be more appropriate to use a third party, but for stakeholder engagement the use of third parties fails to help embed sustainability efforts into the core of the company since the company itself is removed from the stakeholder engagement.[262] There may however be a history of conflict between the company and the stakeholders, and in those cases the use of appropriate third-party mediators may be preferrable and even aid in bridging gaps if a neutral local third party is chosen.[263] Using third parties should however not be the long-term strategy, but rather a short-term tactic to establish report and communication.[264]

5.3.2 OECD Due Diligence Guidance

Pursuant to the OECD Due Diligence Guidance, the level on which stakeholder engagement can be performed varies in part depending on the stability of the region in which a company operates. If *e.g.* the company in question

[255] UNGP Interpretive Guide Q 30.
[256] UNGP Interpretive Guide Q 30.
[257] UNGP Interpretive Guide Q 30.
[258] UNGP Interpretive Guide Q 42.
[259] UNGP Interpretive Guide Box 5.
[260] UNGP Interpretive Guide Box 5.
[261] UNGP Interpretive Guide Q 33.
[262] UNGP Interpretive Guide Q 33.
[263] UNGP Interpretive Guide Q 33.
[264] Compare UNGP Interpretive Guide Q 33.

wishes to conduct consultations in an unsafe region, the safest way may be to consult with bilateral aid agencies (so called donor agencies).[265] Stakeholders in safer, more stable, areas of operations can instead be engaged with on a direct basis.[266] Meaningful stakeholder engagement entails two-way communication performed in good faith.[267] The engagement does not have a set definition but rather comes in the form of hearings, consultations and meetings.[268] Since the engagement of stakeholders is responsive (*i.e.* actively listening to stakeholders) and on-going, stakeholders ought to be consulted prior to major decisions which may impact them.[269]

The engagement being a two-way endeavour entails that stakeholders, as well as the company itself, are provided room for voicing their perspectives and seek differences in those in order to find common ground.[270] Good faith engagement refers to the intentions of the company, *i.e.* that they are founded on genuine interest in reaching common ground and gaining insight into the stakeholder perspective.[271] The good faith is expected to come from both sides, meaning that the stakeholders provide their genuine concerns and the company addresses their potential adverse impacts in an honest way.[272]

When attempting to engage stakeholders who may be vulnerable to an adverse impact, the company should strive towards erasing or minimising barriers that may come in the way of meaningful engagement. These barriers may be cultural, gender based, based on language or rifts in the stakeholder community.[273] It is therefore important to gauge for vulnerable voices in relevant stakeholder groups to ensure that they don't get lost in the general demographic, and prepare to share information with the stakeholders in their language in a way that is appropriate pursuant to their circumstances, for example by way of oral engagement in areas of low literacy.[274]

5.3.3 OECD Apparel Guide

As an example of more sector-specific due diligence guidance regarding stakeholder consultations, the following outlines central provisions embedded in the OECD Apparel Guidance. The due diligence process should encompass meaningful engagement with affected stakeholders. Companies should aim for a two-way engagement performed with attention to responses

[265] OECD Due Diligence Guidance 2018, table 4.
[266] OECD Due Diligence Guidance 2018, table 4.
[267] OECD Due Diligence Guidance 2018, Q9.
[268] OECD Due Diligence Guidance 2018, Q9.
[269] OECD Due Diligence Guidance 2018, Q9.
[270] OECD Due Diligence Guidance 2018, Q9.
[271] OECD Due Diligence Guidance 2018, Q9.
[272] OECD Due Diligence Guidance 2018, Q9.
[273] OECD Due Diligence Guidance 2018, Q11.
[274] OECD Due Diligence Guidance 2018, Q11.

(*i.e.* responsive engagement) and performed in good faith.[275] The stakeholders should be provided with a venue for receiving honest and non-censored (*i.e.* complete) facts related to the company's operations where they may be impacted, and the stakeholders should be provided with the opportunity to voice their opinion and feedback before big decisions are made that may affect them.[276] Aside from providing information on meaningful stakeholder engagement, the OECD Apparel Guidance, like the other sectoral guidance from the OECD, provides unique definitions of stakeholders suited for the particular sector's stakeholders. In the garment and footwear industry, these are *inter alia* direct employees of the company, workers performing for the benefit or on the behalf of the company and suppliers to the company etc.[277]

The OECD Apparel Guidance points to the individual circumstances surrounding a company and its stakeholders as a source for variety in the way stakeholder engagement is conducted. The best method of engagement is likely to be the one that the company and the stakeholders together find agreeable and that works given their specific circumstances.[278] Embedded in this is the need for companies to prioritise the engagement to the favour of stakeholders that run the highest risk of being subjected to adverse impacts on account of the company's operations.[279]

5.4 Supply Chain Upgrades

Global value chains provide for an opportunity for developing nations to be included in economic growth.[280] A sustainable development path that has shown to be viable for large companies is the transfer of technology and knowledge to global value chains.[281] Social upgrading entails engagement with stakeholders on a managerial and directorial level, aimed at making profound improvements in a business partner's operation processes.

"Upgrades" can entail improvements in processes which lead to more profitability or more sophisticated methods of gaining capital through development of skill.[282] Another definition sees upgrades as the shift from low to high-value economic activities using local innovation into functions, products, or processes.[283] The definitions seem to be complementing each other rather than being mutually exclusive. There could therefore be overlap in the application of either definition. Combining the methods could provide for added value. Upgrading can be divided into two attributes; intrinsic (such as product

[275] OECD Apparel Guidance 2018, page 27.
[276] OECD Apparel Guidance 2018, page 27.
[277] OECD Apparel Guidance 2018, page 27.
[278] OECD Apparel Guidance 2018, page 28.
[279] OECD Apparel Guidance 2018, page 28.
[280] Ponte, Gary & Gale (2021), page 282.
[281] Ponte, Gary & Gale (2021), page 282.
[282] Van Dijk & Trienekens (2012), Page 239.
[283] Van Dijk & Trienekens (2012), Page 237.

design, quality and chemical composition) or extrinsic (*e.g.*, the characteristics of the production process).[284]

Western consumers have become more attentive to the extrinsic attributes of a value chain, *e.g.,* prevalence of forced labour, health and safety conditions, child labour etc., which has helped pave the way for voluntary sustainability efforts in western industries.[285] Adding value to extrinsic attributes can help the companies in the value chain gain more independence and control of their production process which makes them more profitable and, hopefully, more prone to reinvest in their own processes.[286] As regards health and safety, value may be added by automating dangerous processes previously done by hand, transferring knowledge on fire hazards in factories, performing audits of business partners, or expanding and improving on the information and communication technology in the operations.[287]

5.5 Discussion

Meaningful stakeholder engagement is not easily defined since both stakeholder and engagement are terms that carry many different values. What is meaningful engagement is also dependent on the circumstances of each individual relationship. Social auditing provides a way for Companies to engage with business partners on a corporate level, which is also important stakeholder engagement, but utilizing social auditing alone does not provide for insight into the conditions of vulnerable stakeholders.

Moreover, social auditing has historically displayed an inability to successfully identify symptoms of potential adverse impacts.

Including the perspectives of vulnerable stakeholders in the identification process of adverse impacts is not only helpful when value chains are mapped out, but also illuminates hidden conflicts and marginalised stakeholders in them.

Stakeholder consultations are therefore, on the face of it, more responsive to the immediate surroundings of the most vulnerable stakeholder. The social audit, conversely, sometimes fails to address potentially severe adverse impacts. It may however provide for a more solution-oriented engagement immediately since vulnerabilities may be addressed on a formal level, while stakeholder consultations on a lower level may entail a lot of social navigation, dispute resolution and cultural reconciliation. Stakeholder consultations may also be prone to inefficiencies if they are executed without responsive two-way communication.

[284] Van Dijk & Trienekens (2012), Page 239.
[285] Van Dijk & Trienekens (2012), Page 239.
[286] Van Dijk & Trienekens (2012), Page 236–237.
[287] Compare Van Dijk & Trienekens (2012), Page 240.

Thorough stakeholder consultations can also be problematic and present issues for the company that they need to internalise. For instance, adapting the stakeholder engagement to the specific circumstances of that stakeholder group's culture may entail that companies adapt to discriminatory practices. For instance, in order not to lose the female perspective in a culture that is prone to deep-rooted systematic gender discrimination, stakeholder consultations could be divided into separate sessions for men and women respectively. This would in practice validate the sexist or otherwise discriminatory structures of that culture but may be the only feasible way to provide a venue for that specific stakeholder profile to voice their concerns. A *prima facie* comparison between commercially oriented social audits and people-focused stakeholder consultations indicate that the latter is more conducive to meaningful engagement. This is however an oversimplification since social auditing provides a channel for direct and lean communication and would be an instrumental component of achieving effective social upgrades.

Moreover, consultations are, as illustrated above, also a possible source of risk. Cultural norms can prohibit certain stakeholder profiles from joining the consultations, *e.g.,* discrimination based on disability, gender expression, gender, racial or caste-based discrimination, *etc*. Moreover, the formalistic nature of social audits makes it easier to have a real-time overview of what compliance measures have been verified, while consultations require a lot of attentiveness and responsiveness during the consultations so as not to exclude relevant perspectives. Social audits therefore provide for an efficient way of communication between a Company and its business partner, but relying too much on formal requirements and whether they are met can cause an overly formalistic, "box-ticking", approach to human rights due diligence that risks alienating stakeholders.

Meaningful stakeholder engagement, in summary, is attentive and responsive to individual voices and inclusive of marginalised voices. It is sensitive to social, economic, and cultural circumstances between and within groups of stakeholders. Meaningful stakeholder engagement is also responsive of, and seeking out, management-level engagement and should aim to use formal and informal methods of building report and communication with stakeholders. Naturally, it is important to include even more channels for stakeholder dialogue, such as *e.g.,* accessible grievance mechanisms.

6 Stakeholder Engagement in the Council's Proposal

6.1 Direct or Indirect Business Partner?

A direct business partner means a legal entity with whom the Company has a commercial agreement with pertaining to provision of services, products, or the operations of the Company.[288] An indirect business partner is a legal entity that performs operations related to the operations of the Company, but without being a direct business partner.[289] An example of a direct business partner could be a factory with an agreement to produce products for a Company. If instead those same products were purchased from a supplier rather than from the manufacturer directly then the factory would be an indirect business partner to the Company.

If a potential adverse impact is identified and presents a need for complex measures to appropriately prevent it, a prevention action plan needs to be set up and implemented without undue delay and with reasonable and defined timelines for actions, as well as a system for measuring improvements in both a qualitative and quantitative sense.[290] To ensure that business partners are compliant with codes of conduct and the potential prevention action plans, companies shall seek such contractual assurances from direct business partners and in turn that the direct business partner seeks corresponding assurances from its partners, if they are linked to the company's chains of activities.[291] Regarding indirect business partners, contracts will be required to be concluded if an adverse impact has been identified but cannot be successfully prevented or adequately mitigated, and the aim of those contracts are the same as for contractual assurances from direct business partners, *i.e.,* adherence to a prevention action plan or CoC.[292] This means, in essence, that Companies will be required to seek contractual assurances from their direct business partners around the time of the adoption of the prevention action plan, while the indirect business partner may be sought after in that regard when other preventive and mitigative efforts have failed.

This could lead to a delayed response to potential adverse impacts where they occur in the operations of an indirect business partner since the Proposal provides that they may be sought after when other preventive measures have been attempted and failed.

[288] The Council's Proposal Article 3.e.i.
[289] The Council's Proposal Article 3.e. ii.
[290] The Council's Proposal Article 7.2.
[291] The Council's Proposal Article 7.2.b.
[292] The Council's Proposal Article 7.3.

The *commercial agreement* between the legal entity in question and the Company is what establishes whether the legal entity is a direct business partner.[293]

This raises the question whether *e.g.,* promises to adhere to a set of demands pursuant to a social audit (before a potential adverse impact has been identified) would constitute a commercial agreement related to the operations, services, or products of the company. Moreover, secured contracts related to adherence to a prevention action plan or CoC pursuant to the provisions discussed (*i.e.,* after a potential adverse impact has been identified) could be interpreted as commercial agreements if they would require investment from the business partner contingent on continued business. There is no official legal definition for the term "commercial agreement" in the EU.[294] This raises further questions as to whether *e.g.,* the commercial agreements can be orally concluded or if they need to be written, pertain to certain commercial interests or otherwise follow a certain format. The term "agreement" is defined but is dependent on the context wherein it is used and can refer to both written and verbal agreements.[295] The lack of clarity would therefore require further guidance from the Commission on the intended scope embedded in "commercial agreement".

6.1.1 Discussion

Seeking contractual assurances from business partners is an effective way to formally engage with stakeholders on a management level. Obligations and responsibilities that may have been neglected or not sufficiently contractually mitigated by the parties can be placed at the front of the relationship and make future cooperation contingent on compliance. Companies may seek to conclude contracts with indirect business partners aimed at securing adherence to a prevention action plan when an adverse impact has been identified and failed to have been adequately prevented or mitigated by way of *e.g.,* targeted support. Direct business partners, on the other hand, must be sought after by the Companies already at the identification stage.

Placing the responsibility to collect assurances from indirect business partners *after* other preventive and mitigative efforts may prolong the exposure of potentially affected stakeholders to the risks associated with the potential impact. Delayed contractual assurances from indirect business partners can lead to necessary actions not being taken by the indirect business partner in time to prevent and adverse impact. Moreover, including indirect business partners in the requirement to provide contractual assurances at the identification stages rather than a near-last resort would give companies more control over

[293] The Council's Proposal Article 3.e.i.

[294] Interactive Terminology for Europe, Link: https://iate.europa.eu/home Accessed 19 May 2023.

[295] Interactive Terminology for Europe, Link: https://iate.europa.eu/search/result/1684484147203/1 Accessed 19 May 2023.

preventive and mitigative efforts. The variable scope of the obligation to seek to secure contractual assurances is understandable since any obligation on Companies will require investments on their part. It also provides predictability for both the Companies and their business partners which ultimately benefits compliance throughout the Union.

The distinction between indirect and direct business partners may however give rise to other issues altogether.

For instance, in the case of the Tazreen Fashions factory fire, Walmart[296] had a list of approved manufacturers which included Tazreen Fashions. Pursuant to the definitions of the Proposal, the relationship between Walmart and Tazreen would be considered indirect. It could however be argued that Tazreen Fashions were not as indirect of a partner that a *prima facie* examination would suggest. The auditor is reported to have made demands against Tazreen Fashions regarding a prevention action plan that Tazreen Fashions would have to develop. If non-compliance of that demand would entail exclusion from the list of authorized manufacturers, it could be argued that it was a commercial agreement between Walmart and Tazreen Fashions since the agreement would indirectly pertain to Walmart's operations and products.

If the above circumstances would constitute a commercial agreement, then their business relationship may have qualified as a direct partnership, which lessens the predictability for the Proposal's addressees. Since, however, there is no definition for commercial agreements in the Proposal, the argument stands on a weak foundation. It may very well be that the term refers only to written agreements or that it must be a commercial agreement in the sense that it pertains to commercial *transactions* and not *compliance undertakings*.

The distinction between the types of contracts mentioned can however also provide for ambiguous borders. For example, a SME indirect business partner could be required to make a financial investment into their operations to appease a prevention action plan so as not to lose the business of a Company. In order for the Company to meet its obligation to provide targeted support to business partners, the Company undertakes to continue sourcing from the business partner if it makes the necessary investments. The combined efforts prevent the potential adverse impact, and the partnership continues.

At this stage, there would be grounds for questioning whether the partnership is indirect anymore, or if it has requalified on account of the cooperation.

Unless the Commission elaborates in guidelines how to define a commercial agreement or the Council's Proposal is amended to provide clarity, the act of seeking contractual assurances from indirect business partners could be argued to requalify them as direct, and thereby extend the scope of required actions pursuant to the Proposal.

[296] Note: Walmart is a non-EU company without turnover in the Union and would therefore not be within the scope of the Proposal. The example is only used to illustrate the potential problems in drawing boundaries between direct and indirect business partners.

6.2 Targeted Support

Pursuant to the Proposal, actions required by companies to prevent and mitigate adverse impacts may include investing in management systems, processes, and infrastructure if the business partner is an SME.[297] An "SME" refers to micro, small or medium-sized undertakings regardless of the legal form of the undertaking, that is not part of a large group.[298]

The enumerated measures of targeted assistance which the company is expected to provide to SME business partners is extensive. For instance, they include providing loans to the SME with low interest rates or even direct financing. [299] It may also be in the form of guarantees to extend sourcing agreements, or it could be in the form of non-financial support such as knowledge transfers or upgrading management processes.[300]

6.2.1 Discussion

The measures that may become relevant for companies when preventing adverse impacts includes both financial and non-financial investments into management or production processes. The targeted measures are therefore similar to the extrinsic process upgrades discussed in Section 5.4. The targeted and proportionate support is aimed at assisting a SME business partner in complying with the CoC of prevention action plan and is relevant when it cannot viably do so by its own means. Moreover, the exemplified support is very wide since it envelops direct financing, training, low-interest loans and upgrading management systems. Since the potential adverse impact can vary in regard to measures necessary for its prevention or mitigation, the range of possible support methods varies accordingly. Since the necessary support could be minor or so extensive as to warrant termination of the business relationship, it is not easy to analyse its potential effect.

What a necessary financial or non-financial investment is can be assessed only when the potential adverse impact has been identified and the prevention action plan has identified what measures must be taken to adequately prevent it. It is unlikely that it would entail renovating entire dilapidated factories since, even if that factory was part of the operations of a SME direct business partner, the matter of proportionality and other measures of the proposal (see Section 6.3 on termination of business relationships below) would make such extensive measures essentially voluntary.

[297] The Council's Proposal Article 7.2.d.
[298] The Council's Proposal Article 3.i.
[299] The Council's Proposal Article 7.2.d.
[300] The Council's Proposal Article 7.2.d.

This is proportionally sound mechanisms since it would be too burdensome to require companies to vertically integrate severe potential adverse impacts into their operations. For instance, assume that a SME business partner operates in facilities that have been found to be structurally unsound, and the impact assessment during the development of the prevention action plan indicates that the adverse impact can only be prevented by leaving the building entirely. This would indicate that the potential adverse impact is not only severe (and the partnership should therefore be terminated) but would also reasonably require a long-term solution (which is also grounds for termination of the business relationship).

Unless the company could argue then that the adverse impact would become more severe if the relationship was terminated, or that it would cause the Company substantial prejudice to their operations, then the Proposal would demand termination, rather that targeted support. As the example above indicates, the outer reaches of targeted support pursuant to the mechanisms of the Proposal are reached when the preventive measures are expected to be long-term. After that point, Companies would have to take a defensive position *vis-à-vis* supervisory authorities in order not to be required to terminate a business relationship as described. This is problematic since the wide scope of the provision on targeted support promotes creative collaboration between companies to reach effective and proportionate support, but adjacent mechanisms pertaining to termination instead incentivise termination of those relationships.

6.3 Suspension and Termination of Relationships

If a potential adverse impact has been identified and it is not possible to prevent it or mitigate it sufficiently by the means provided above, the company must, as a last resort, refrain from extending business relationships or entering new ones with business partners involved in or otherwise active in the chains of activities of that adverse impact.[301] The obligation to terminate a business relationship is a last resort since termination on account of a business partner's supply chain containing *e.g.* child labour may lead to an exacerbation of the child labourers situation.[302] The same reasoning would be transposable in cases of mismanagement of environmental matters, poor health and safety compliance, forced labour etc. When a potential adverse impact has been identified in a business partner's operations, a Company must first suspend the relationship during the efforts to bring the adverse impacts to an end.[303]

The above applies only if it is reasonable to expect that such efforts will be successful in the short term. If short term expectations of mitigation are

[301] The Council's Proposal Article 7.5, para 1.
[302] The Commission's draft, Recital 32.
[303] The Council's Proposal Article 7.5.a.

unreasonable, the relationship must be terminated.[304] If the identified potential adverse impact is severe, then the business relationship must be terminated regardless of the duration of time it will take to prevent or mitigate it.[305] Member States will be required to provide legal options for Companies to suspend and terminate business relationships except for certain contracts that parties are legally obligated to enter into.[306] The contracts referred would be *e.g.* mandatory insurance contracts.[307]

There are however ways for companies to stay in the business relationships described above. If the act of termination of a business relationship entails reasonable expectations of the adverse impact becoming even more severe, then the obligation to terminate does not apply.[308] Likewise, if the business partner to the Company is an essential provider of services or products, and termination of the business relationship would be detrimental [cause substantial prejudice] to the Company's commercial viability, then the Company shall not be required to terminate it.[309] Substantial prejudice is significant negative effects on a Company regarding, *inter alia*, its finances, production capacity and long-term solvency.[310]

Aside from reporting the decision and reasons for not terminating the business relationship to a competent supervisory authority, the company is also obligated to continually monitor and reassess its decision. .[311] It must also seek alternative business partners to engage.[312] The supervisory authorities in each Member State are provided power to request information and investigate companies regarding their compliance with the due diligence requirements.[313]

6.3.1 Discussion

Termination is framed as a last resort in the recitals, but in practice the mechanisms of termination of a business relationship are prominent since the Proposal does not require that termination be reported to supervisory authorities (only non-termination must be reported). Moreover, Member States are required to ensure that business relationships can be terminated and suspended, with the exception being certain specific contracts mandated by law to be entered, such as mandatory insurance contracts. This makes the decision to terminate a business relationship subject to adversity even more accessible.

[304] The Council's Proposal Article 7.5.a.
[305] The Council's Proposal Article 7.5.b.
[306] The Council's Proposal Article 7.5, para 2.
[307] The Councils Proposal Recital 36.
[308] The Council's Proposal Article 7.7.a.
[309] The Council's Proposal Article 7.7.b.; Recital 36a.
[310] The Council's Proposal Recital 36a.
[311] The Council's Proposal Articles 7.7, para 2 and 7.7, para 3.
[312] The Council's Proposal Articles 7.7, para 2 and 7.7, para 3.
[313] The Council's Proposal Article 18.1.

The decision to terminate a business relationship is seemingly left to the discretion of in-scope Companies. This is not controversial since companies have an interest in avoiding association with adverse impacts. From a stakeholder-perspective however, termination is unsatisfactory since it does not resolve the potential adverse impacts. Ideally, rather than terminating business relationships, companies ought to be empowered and incentivised by the Proposal to seek to maintain the relationships in faltering supply chains and work to assist their stakeholders in appropriate and proportionate ways pursuant to the extent of the relationship.

Since the Proposal contains elements of social upgrading, one could be led to assume that there would be safeguards implemented to ensure that Companies do not exploit supply chain links and then abandon them if they are uncovered. A Union-wide mechanism for terminating business partnerships with identified potential adverse impacts in their operations is instead introduced in the Proposal. When it comes to decisions *not* to terminate business relationships, however, safeguards are implemented. Regardless of whether a Company claims that the relationship cannot be terminated on grounds of exacerbation or substantial prejudice, the company has an obligation to continually reassess the decision, monitor the potential adverse impact and actively seek alternative business relationships (which embeds yet another incentive to terminate business relationship). There is no such requirement to evaluate and monitor decisions to *terminate* a business relationship on account of an identified adverse impact.

Supervisory authorities are however empowered to request information and conduct investigations into companies regarding their compliance with the due diligence requirements, so there is room for safeguards regarding decisions to terminate business relationships. This is however not entirely unproblematic. If an adverse impact occurs in the operations of a terminated business partner that could reasonably have been prevented if the partnership had not been broken up, and the supervisory authority of the country in question pursues an investigation, then it is obviously not proactive supervision, but rather reactive. While such an approach is conducive to remediation, it fails to assume supervisory control over the antecedent stages of an adverse impact.

The decisions are left to the personal discretion of Companies to make as regards termination, suspension or neither. This is understandable from an economic perspective, considerations to reputational risk, and the risk-based approach to human rights due diligence but is nonetheless grounds for concern since it can diminish the impact of sustainability development. Not least does it risk making measures such as targeted support ineffective, as is shown above.

It also risks recreating incidents such as the Walmart – Tazreen Fashions situation where Walmart abandoned its business partner, and the potential adverse impact was later actualised. The Proposal, as it is devised now, would facilitate the same circumstances by offering an in-scope Company the option of terminating a partnership in line with the provided circumstances of the Tazreen Fashions tragedy. Companies are however empowered to remain in business relationships with potential adverse impacts identified if termination would cause the company substantial prejudice or exacerbate the adversity. Such a decision not to terminate is however contingent on continual monitoring, evaluation and reporting which may disincentivise Companies.

To summarize, the available instruments for both measures (termination and non-termination respectively) generally provide for a balanced set of alternatives for a Company when faced with an adverse impact in a business partner's operations. The possible implications of termination of business partnerships are however understated but likely have reasonable motivations rooted in consideration for corporate discretion, proportionality, risk-based human rights due diligence etc.

7 Research Conclusions

(i)

Is Hard Law Necessary for the Promotion of Business and Human Rights?

Even though established soft law such as the UNGP has authority by means of its endorsement by the United Nations and other normative sources discussed above, the voluntary actions companies take based on that authority still fall short of creating predictable compliance. Business and human rights soft law is not legally binding on any companies unless they have contractually submitted to enforceable measures. Mechanisms for enforcement must therefore be sought on a voluntary basis.

Institutions such as the OECD's National Contact Points are enabled by companies on a voluntary basis. They aim to provide for enforcement by utilizing social pressure on companies to engage in mediations. The efficacy of the mediations taking place in the NCPs is however limited since the procedures are voluntary on companies and the mediations themselves risk being politicized depending on *e.g.,* which governmental body hosts the NCP of the State in question. The main source of incentives for companies regarding voluntary participation in the mediations is that the NCP may issue a public statement wherein the background to the dispute, positions of the parties and recommendations of the OECD are presented, effectively naming and shaming businesses who fail or refuse to participate in mediations.

This has proved to be ineffective since seven out of eight mediations result in outcomes that the parties find unsatisfactory, indicating that social pressure alone cannot promote sustainable enforcement of business and human rights. The overall lack of enforcement power in soft law instruments curtails the impact of business and human rights soft law and their enforcement mechanisms, if any are embedded in them. System-wide compliance requires business and human rights law that is enforceable and inherently mandatory. Based on the foregoing, business and human rights hard law is necessary for the enforcement of business and human rights law. The investigation shows, however, that hard law is not necessary for the promotion of business and human rights law, since the impetus for the hard law was, indeed, soft law.

(ii)

What Role Should Soft Law Have in the Context of Emerging Hard Law?

Transitioning to hard law provides tools for state enforcement but is not in itself sufficient for sustainable growth, since any meaningful change ought to have been internalised by the private sector as well. Appreciating the utility provided in the mixture of sources of normativity that makes up the constitution of business and human rights soft law is therefore imperative in the continued evolution of responsible business conduct. The impact soft law can have is evident by the magnitude of influence the UNGP has had on business and human rights, proving that enforcement, which can be achieved by way of voluntarism, is not the determining factor for spreading responsible business conduct. Understanding this is key moving forward, since legislating and enforcing a rule does not mean that the issue is systemically cleansed, nor does the enforceability of a given rule mean that it will lead to meaningful compliance. It would therefore be unhelpful for the promotion of business and human rights law to dismiss the continued utility of soft law inside and outside the Union. This is where the issues from changing the meaning of established business and human rights soft law comes into play (*i.e.,* value chains of activities instead of value chain).

In order not to exacerbate existing disparities in the international business and human rights context, adopted hard law ought to be in line with established soft law such as the Guiding Principles and OECD instruments. Deviating too much can create new schisms in the international human rights community and potentially stifle the evolution of business and human rights altogether.

(iii)

Are the Provisions of the Proposal Conducive to Meaningful Stakeholder Engagement?

The differentiation made between direct and indirect business partners in the Proposal facilitates proportionality in the responsibilities placed on Companies *vis-à-vis* their business partners. There is however some ambiguity as to what commercial agreements are, which is problematic since entering into those agreements is a qualifier for direct partnerships. In the absence of guidance, it could be argued that contracts related to adherence to a prevention action plan may be commercial agreements. For example, such adherence could be contingent on investments from the business partner into financing process upgrades. The Company could provide guarantees of continued business as an incentive (which, if proportionate, would fall under the Company's responsibility to provide targeted support).

The above mentioned could be construed as a commercial agreement, thereby raising the issue of whether the relationship is requalified as direct rather than indirect. The ambiguity could lessen the predictability of the legal effect. This ambiguity would however, if not disproven or mitigated by means of guidelines or clarifications from the Commission, work in the stakeholder's favour since it would provide civil rights organisations room for arguing that indirect business partnerships should be requalified, thereby granting the business partner and its employees more rights *vis-à-vis* the Company. Such uncertainties fail however in providing predictability for both a Company and its stakeholders. If a partnership could requalify as direct by means of contractual assurances as described above, the extended rights catalogue provided to the stakeholder is likely not an intended effect. Any additions to the material protection a stakeholder gets from a Company would therefore be incidental. The Commission ought to issue guidance on the interpretation of the term commercial agreement since the lack of legal clarity is detrimental to transparent stakeholder engagement.

The required targeted support to SME business partners that cannot viably comply with the demands of a prevention action plan and CoC following an identified potential adverse impact is extensive. The supporting measures are not divided into segmented tier-based systems like the scope of the identification measures, instead it promotes free expression of creative solutions to problems defined in prevention action plans. The provision that lays down the rules for targeted support cannot be said to focus on either extrinsic or intrinsic upgrading methods. The measures required instead depend on what the prevention action plan requires from the parties. So, the quality of the chosen method of supporting is anchored in the profoundness of the prevention action plan and its implementation. The very minimum assistance that would come into play (if any assistance would be proportionate at all) is whatever measures helps the business partner adhere to a prevention action plan. The proportionality also limits the scope of required assistance as regards extensiveness. The article itself is therefore materially satisfactory, since it provides ample opportunity for creativity, and minimal limitations in practice. The issue lies instead in the Proposal's tendency to promote termination of business relationships. Naturally, this is a part of a risk-based approach to human rights due diligence where complicity or indifference to violations of human rights is not tolerated. This may however lead to situations where adverse impacts that could have been averted instead becomes actual because of the Union legislator's eagerness to eject EU-companies from mitigation-efforts rather than confront them. To summarize, what constitutes proportionate targeted support depends entirely on what the prevention action plan demands from the parties involved and is heavily dependent on the assessment pursuant to the suspension and termination clauses of the Proposal. The mechanisms embedded in the requirement to provide targeted assistance to an SME is dynamic and facilitates meaningful stakeholder engagement. Another issue which takes away from the aforementioned is the mechanisms of termination of business relationships.

An overreliance on termination mechanisms in the face of adversity works to the detriment of the overall impact of stakeholder engagement facilitated by the Proposal. On the face of it, termination is framed a last resort. However, the instruments provided to Companies if they'd like to terminate a business relationship are more accessible than mechanisms of non-termination. Supervisory authorities will be granted power to request information and conduct investigations, but their activities risk becoming reactive rather than proactive since it is reasonable to expect that a wrongfully terminated business relationship will sometimes have a delayed visibility as regards the subsequent adverse impact.

Moreover, targeted assistance to SMEs will no longer be required if the Company asserts that the potential adverse impact may be severe, or that prevention or mitigation would not be manageable in the short-term. There is a risk of the provisions of the Proposal facilitating the recreating of the Tazreen Fashions incident. If indeed a Company would identify extensive hazards related to health and safety that could potentially cause fatalities if actualised, then the potential adverse impact would be deemed severe. This would, as a rule, require termination of the business relationship on the part of the Company. Fundamentally, however, the balance between the mechanisms for and against termination are sound. Companies can decide not to terminate a business relationship pursuant to concerns of the termination exacerbating the issues. Whether Companies will utilize this possibility for philanthropic social upgrades remains to be seen, but the Proposal allows for these possibilities regardless.

The biggest source of the uncertainties provided above is the lack of clear instruction from the Union legislator. More guidance will be required from the Commission to provide clarity and legal certainty into the provisions investigated.

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