Publications of the Ministry of Economic Affairs and Employment
• Enterprises • 2020:44

Judicial Analysis on the Corporate Social Responsibility Act

Ministry of Economic Affairs
and Employment of Finland

Publications of the Ministry of Economic Affairs and Employment 2020:44

Judicial Analysis on the Corporate Social Responsibility Act

Ministry of Economic Affairs and Employment, Helsinki 2020

Note on the translation

This is an unofficial and in large parts a verbatim translation of a judicial analysis on the possibility of enacting a Corporate Social Responsibility Act Finland, originally written in Finnish and with the Finnish regulatory framework in mind. Owing to the verbatim nature of the translation, we recognize there may be some inconsistencies in the use of terminology and would especially like to make following observations.

In Finland, the terms Corporate Social Responsibility and Corporate Responsibility are generally used to refer to a company's responsibility on its impacts on society, the environment, and the economy. While we acknowledge these terms may have a different meaning especially in an Anglo-Saxon context, we keep to these as these were the terms used in the Governmental Programme where this study derives from. Responsible business conduct is used in reference to the European Union or to the OECD.

The term 'due diligence' used in the UN Guiding Principles and the OECD Guidelines has in the Finnish versions of the text been translated using the term 'duty of care' (*huolellisuusvelvoite* or *asianmukainen huolellisuus*). As due diligence could be framed as duty of care in legislation, these terms are used interchangeably in this report.

Ministry of Economic Affairs and Employment

ISBN PDF: 978-952-327-553-9

Layout: Government Administration Department, Publications

Helsinki 2020

Description sheet

Published by	Ministry of Economic Affairs and Employment		2 September 2020
Authors	Ernst & Young Oy: Sakari Helminen, Jani Alenius, Ville Walta, Sofia Donner		
Title of publication	Judicial Analysis on the Corporate Social Responsibility Act		
Series and publication number	Publications of the Ministry of Economic Affairs and Employment 2020:44		
Register number	TEM045:00/2020	**Subject**	Enterprises
ISBN PDF	978-952-327-553-9	**ISSN (PDF)**	1797-3562
Website address (URN)	http://urn.fi/URN:ISBN:978-952-327-553-9		
Pages	113	**Language**	English
Keywords	enterprises, businesses, legislation, human rights, environment, due diligence, social responsibility, corporate responsibility		

Abstract

Ernst & Young Oy has prepared a judicial analysis on the Corporate Social Responsibility Act commissioned by the Ministry of Economic Affairs and Employment. The analysis outlines the nature of the due diligence obligations that could be imposed on companies within a legislative framework in Finland. Due diligence refers to the process in which a company identifies, prevents and mitigates real and potential adverse impacts on human rights and the environment in its own activities, supply chain and other business relationships. The report explores possible regulatory options, their scope of application, supervision and sanctions under corporate social responsibility legislation. An analysis of corporate social responsibility regulation in the European Union and some other countries provides a backdrop for the report.

According to the analysis, business operations are already subject to various due diligence obligations, which require companies to assess and prevent risks associated with their operations. It would be possible to impose a duty of due diligence on companies regarding the environment and human rights within the framework of the national legal system. However, there are a number of issues to consider in relation to the legislation.

The preparation process of this analysis was guided by a steering group that involved the Ministry of Economic Affairs and Employment, the Ministry for Foreign Affairs, the Ministry of Justice, the Ministry of the Environment and the Ownership Steering Department of the Prime Minister's Office. The Committee on Corporate Social Responsibility acted as an advisory body.

This analysis is included in the Government Programme and Action Plan of Prime Minister Marin's Government.

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Publisher	Ministry of Economic Affairs and Employment
Distributed by/ publication sales	Online version: julkaisut.valtioneuvosto.fi Publication sales: vnjulkaisumyynti.fi

Kuvailulehti

Julkaisija	Työ- ja elinkeinoministeriö		2.9.2020
Tekijät	Ernst & Young Oy: Sakari Helminen, Jani Alenius, Ville Walta, Sofia Donner		
Julkaisun nimi	Oikeudellinen selvitys yritysvastuulaista		
Julkaisusarjan nimi ja numero	Työ- ja elinkeinoministeriön julkaisuja 2020:44		
Diaari/hankenumero	TEM045:00/2020	**Teema**	Yritykset
ISBN PDF	978-952-327-553-9	**ISSN PDF**	1797-3562
URN-osoite	http://urn.fi/URN:ISBN:978-952-327-553-9		
Sivumäärä	113	**Kieli**	englanti
Asiasanat	Yritykset, elinkeinot, lainsäädäntö, ihmisoikeudet, ympäristö, huolellisuus, yhteiskuntavastuu, yritysvastuu		

Tiivistelmä

Ernst & Young Oy on tehnyt oikeudellisen selvityksen yritysvastuulaista työ- ja elinkeinoministeriön tilauksesta. Selvitys kartoittaa, millainen yrityksille lainsäädännössä asettava asianmukaisen huolellisuuden velvoite voisi olla Suomessa. Asianmukaisella huolellisuudella tarkoitetaan prosessia, jolla yritys tunnistaa, ehkäisee ja lieventää todellisia ja mahdollisia haitallisia vaikutuksia ihmisoikeuksille ja ympäristölle omassa toiminnassaan, toimitusketjussaan ja muissa liiketoimintasuhteissaan. Selvityksessä avataan yritysvastuulain mahdollisia sääntelyvaihtoehtoja, soveltamisalaa sekä valvontaa ja sanktioita. Tarkastelun taustaksi selvityksessä käydään läpi Euroopan unionin sekä eräiden muiden maiden yritysvastuusääntelyä.

Selvityksen mukaan yritystoimintaa kohdistuu jo nykyisellään erilaisia huolellisuuden velvoitteita, joilla yrityksiä velvoitetaan arvioimaan ja ehkäisemään niiden toimintaan liittyviä riskejä. Yrityksille asetettavan ympäristöä ja ihmisoikeuksia koskevan huolellisuuden velvoitteen säätäminen olisi kansallisen oikeusjärjestelmän puitteissa mahdollista. Lainsäädäntöön liittyy kuitenkin useita harkittavia kysymyksiä.

Selvityksen tekoa ohjasi ohjausryhmä, jossa olivat mukana työ- ja elinkeinoministeriö, ulkoministeriö, oikeusministeriö, ympäristöministeriö sekä valtioneuvoston kanslian omistajaohjausosasto. Yhteiskunta- ja yritysvastuun neuvottelukunta toimi selvityksen neuvoa-antavana elimenä.

Selvitys sisältyy pääministeri Marinin hallitusohjelmaan ja toimintasuunnitelmaan.

Työ- ja elinkeinoministeriön yhdyshenkilö: Työllisyys ja toimivat markkinat/ Erityisasiantuntija Linda Piirto, puh. 029 50 47028

Kustantaja	Työ- ja elinkeinoministeriö
Julkaisun jakaja/myynti	Sähköinen versio: julkaisut.valtioneuvosto.fi Julkaisumyynti: vnjulkaisumyynti.fi

Presentationsblad

Utgivare	Arbets- och näringsministeriet		2.9.2020
Författare	Ernst & Young Oy: Sakari Helminen, Jani Alenius, Ville Walta, Sofia Donner		
Publikationens titel	Juridisk utredning om en lag om företagsansvar		
Publikationsseriens namn och nummer	Arbets- och näringsministeriets publikationer 2020:44		
Diarie-/ projektnummer	TEM045:00/2020	**Tema**	Företag
ISBN PDF	978-952-327-553-9	**ISSN PDF**	1797-3562
URN-adress	http://urn.fi/URN:ISBN:978-952-327-553-9		
Sidantal	113	**Språk**	engelska
Nyckelord	företag, näringsgrenar, lagstiftning, mänskliga rättigheter, miljö, omsorg, samhällsansvar, företagsansvar		

Referat

Ernst & Young Oy har gjort en juridisk utredning om en lag om företagsansvar på beställning av arbets- och näringsministeriet. Utredningen kartlägger vilken skyldighet att iaktta tillbörlig aktsamhet företagen kunde ha i lagstiftningen i Finland. Med tillbörlig aktsamhet avses en process genom vilken ett företag identifierar, förebygger och lindrar faktiska och potentiella skadliga konsekvenser för de mänskliga rättigheterna och miljön i sin egen verksamhet, leveranskedjan och andra affärsrelationer. Utredningen redogör för eventuella regleringsalternativ, tillämpningsområde samt tillsyn och sanktioner för lagen om företagsansvar. Som bakgrund till granskningen går utredningen igenom regleringen om företagsansvar i Europeiska unionen och i vissa andra länder.

Enligt utredningen omfattas företagsverksamheten redan nu av olika omsorgsskyldigheter, genom vilka företagen åläggs att bedöma och förebygga de risker som är förenade med deras verksamhet. Det är möjligt att införa en skyldighet för företag att iaktta omsorg om miljön och de mänskliga rättigheterna inom ramen för det nationella rättssystemet. Det finns dock flera frågor kring lagstiftningen som bör övervägas.

Utredningen styrdes av en styrgrupp där arbets- och näringsministeriet, utrikesministeriet, justitieministeriet, miljöministeriet och avdelningen för ägarstyrning vid statsrådets kansli deltog. Delegationen för samhälls- och företagsansvar var ett rådgivande organ för utredningen.

Utredningen ingår i statsminister Marins regeringsprogram och handlingsplan.

Kontaktperson vid arbets- och näringsministeriet: Sysselsättning och fungerande marknader / specialsakkunnig Linda Piirto, tfn 029 50 47028

Förläggare	Arbets- och näringsministeriet
Distribution/ beställningar	Elektronisk version: julkaisut.valtioneuvosto.fi Beställningar: vnjulkaisumyynti.fi

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FOREWORD

On 2 October 2019, the Ministry of Economic Affairs and Employment (MEE) issued an invitation to tender for a judicial analysis regarding the possibility of enacting a statutory corporate human rights and environmental due diligence obligation. The contract was awarded to Ernst & Young Oy (EY).

The following aspects are covered in the report:

- due diligence obligations contained in legislation or soft law instruments of other countries and the legislative and soft law projects under way in other countries and at EU level;
- possible content of the corporate due diligence obligation that would be based on international standards for responsible business operations and would apply to human rights and the environment; and
- a judicial analysis of the manner in which a national due diligence obligation could be implemented.

The report has been prepared in accordance with the framework and terms and conditions laid out in the invitation to tender issued by the Ministry of Economic Affairs and Employment and the subsequent agreement. A steering group consisting of the representatives of the Ministry of Economic Affairs and Employment, Ministry of Justice, Ministry of the Environment, Ministry for Foreign Affairs, and the Ownership Steering Department in the Prime Minister's Office was appointed for the work. The steering group met six times during the preparation of the report.

The Committee on Corporate Social Responsibility acted as the advisory body for the work, and the following organisations were represented in the committee: Ministry of Economic Affairs and Employment, Ministry for Foreign Affairs, Ministry of the Environment (deputy member: Ministry of Social Affairs and Health), Ownership Steering Department of the Prime Minister's Office, Federation of Finnish Enterprises,

Confederation of Finnish Industries (EK), ICC Finland, Central Organisation of Finnish Trade Unions (SAK), Finnish Confederation of Professionals (STTK), Akava - Confederation of Unions for Professional and Managerial Staff in Finland, Evangelical Lutheran Church of Finland (deputy member: The Consumers' Union of Finland), FIBS, Finnwatch, Finnish Development NGOs – Fingo, and the Finnish Association for Nature Conservation. The outline for the work was presented to the committee on 29 January 2020, followed by the first preliminary draft on 22 April 2020. The members of the committee were also provided with an opportunity to meet with representatives of EY and to present their views on the topic of the report and the issues that, in their opinion, should be discussed in it.

A stakeholder consultation on the preliminary draft was held on 19 May 2020.

After the report has been finalised, the Ministry of Economic Affairs and Employment will also circulate the document for comments. The English translation of the report is scheduled to be published late August/early September 2020.

EY submits the report to the Ministry of Economic Affairs and Employment on 30 June 2020 and would like to respectfully thank the members of the steering group and the committee for their cooperation. EY is privileged to have had the opportunity to take part in this important project and extends sincere thanks to all those taking part in the stakeholder consultation and parties that submitted opinions and comments during the report finalisation stage.

1 Introduction

1.1 Objectives

This report examines national and international regulation of corporate social responsibility[1] and the human rights and environmental due diligence obligations imposed on enterprises under national law.

Businesses have a major impact on the lives of people in both Finland and other parts of the world. The impacts are not only reflected in the jobs, products and services offered by enterprises but also more broadly in the environmental and human rights impacts of business operations, as well as in employees' working conditions and wellbeing.

Even though business operations have a wide range of positive impacts on society, increasing attention is paid on their potential adverse effects and on preventing them. There are a number of factors behind this development, such as increasing awareness of climate change and the problems caused by it,[2] irregularities uncovered in enterprises, increasing awareness of the potentially adverse impacts of otherwise beneficial business operations,[3] and demands placed on enterprises by consumers and investors.

As a rule, the responsibility for safeguarding human rights and protecting the environment lies with governments, which exercise their responsibility by enacting laws protecting human rights and the environment. Finland has its own legislation on protecting human rights and the environment, which is also binding on companies operating in Finland. In global business operations, the risks associated with human rights and the environment are highlighted when operations and/or supply chains are located

1 In Finland, the terms Corporate Social Responsibility and Corporate Responsibility are generally used to refer to a company's responsibility on its impacts on society, the environment, and the economy. While we acknowledge these terms may have a different meaning especially in an Anglo-Saxon context, we keep to these as these were the terms used in the Governmental Programme where this study derives from. Responsible business conduct is used in reference to the European Union or to the OECD.

2 For example, IPCC report on the impacts of global warming: https://www.ipcc.ch/sr15/.

3 Study on Due Diligence, pp. 214–218; Zerk 2011, pp. 16–30. OECD Guidelines for Multinational Enterprises.

in countries and regions where the national legislation does not offer sufficient protection for employees and the environment or where legislation is not adequately enforced.

To close the regulatory gaps created by multinational business operations, voluntary soft law instruments have been prepared to promote responsible business conduct and to reduce the adverse effects of business operations on human rights and the environment. The most important of these voluntary guidelines are the **UN Guiding Principles** and the **OECD Guidelines for Multinational Enterprises.** Under these guidelines, enterprises should exercise due diligence to identify, prevent and mitigate actual and potential adverse impacts (risks) arising from their operations (including transboundary operations).[4]

The UN Guiding Principles and the OECD Guidelines are part of a broader concept of corporate social responsibility, which is defined by the European Commission as a company's responsibility for its societal impacts. These requirements are also referred to as **corporate responsibility** and **responsible business** conduct.[5]

Some of the voluntary guidelines have also been incorporated into EU-level and national legislation as binding obligations. Until now, the legislative focus has been on regulating particularly high-risk sectors or on introducing provisions obliging enterprises to report on measures that they use to exercise due diligence. France is the only country that has introduced a human rights and environmental due diligence obligation. Provisions on a more limited due diligence obligation are contained, for example, in the Conflict Minerals Regulation of the EU and the Dutch act on child labour. The main explanation for the approach emphasising the reporting obligation is that for many years, corporate responsibility has been seen as a voluntary activity monitored by the markets. Obligatory reporting facilitates monitoring by producing information to the market.[6]

Introducing EU-level legislation on due diligence was examined in a report commissioned by the European Commission and published in spring 2020.[7] A number of EU Member States are also planning to enact due diligence regulation or examining the need for such regulation. Regulation of corporate responsibility has also been discussed in other Nordic countries. However, so far, none of them has adopted corporate social responsibility legislation that includes the obligation to exercise human rights and environmental due diligence.[8]

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4 OECD Due Diligence Guidance for Responsible Business Conduct, p. 15.

5 See OECD Due Diligence Guidance for Responsible Business Conduct; COM(2011) 681; SWD(2019) 143, p. 2.

6 For example, Lautjärvi 2019, pp. 435–437.

7 Study on Due Diligence, p. 41.

8 For Norway, see Study on Due Diligence, pp. 195–196; for Sweden, see Heasman 2020a, pp. 281–295; for Denmark, see Heasman 2020b, pp. 22–37.

The need to redefine the purpose of commercial operations in a manner that in addition to shareholders, would also explicitly take into account all other stakeholders has also been highlighted in the debate on responsible business conduct.[9] In fact, some countries now require that companies must also consider the social and environmental impacts of their operations when fulfilling their statutory purpose of generating profits for their shareholders.[10] The extensive debate on the purpose of business operations is only briefly discussed in this report. This is partly because Finland and a number of other EU countries are currently examining the need to reform the legislation on limited liability companies.

The focus in this report is on a corporate due diligence obligation that would cover the human rights and environment impacts arising from their operations. Corporate social responsibility is closely connected with human rights, the environment, sustainable development, social factors and good governance.[11] There are many legislative projects under way that are at least loosely connected with business operations, human rights and the environment. In these projects the topic is approached from different perspectives and regulatory measures affecting a wide range of different actors are proposed. Examples include regulating institutional investors and banks with the purpose to impact the funding and governance of companies. Good corporate governance can also refer to taxation-related factors. For example, issues pertaining to sustainability in taxation play an important role in the international debate. At the same time, consumer protection legislation provides consumers with information and makes them better placed to influence companies and their products. In fact, regulation of sustainable and responsible business operations would probably require a holistic and supranational approach.[12]

A number of legislative projects on responsibility are briefly discussed in this report. However, the focus is on due diligence legislation and the possible content of the Finnish act on corporate social responsibility that would cover human rights and the environment.

The report also discusses legislation under which companies are obligated to report on exercising due diligence. A review of these laws is necessary to outline the history of and debate on corporate social responsibility legislation, and to describe the content of due diligence and detail some of the existing regulatory solutions. A small number of

9 For example, Annual meeting of the World Economic Forum in Davos (https://www.weforum.org/events/world-economic-forum-annual-meeting-2020) and the statement issued by the US Business Roundtable (https://opportunity.businessroundtable.org/ourcommitment/).

10 For example, France, Article 169 of Loi Pacte; United Kingdom, Section 172 of the Company Act.

11 The term ESG is also a corporate responsibility concept. It stands for *Environmental, Social and Governance* and refers to matters pertaining to corporate environmental and social responsibility and good corporate governance.

12 The European Commission includes legislative projects on privacy protection, taxation, the environment, waste management, consumer protection, companies and credit institutions, and sustainable development in its list of corporate social responsibility legislation; SWD(2019) 143.

legislative drafts and proposals are also discussed to outline the regulatory alternatives presented in the report.

The purpose of the report is to outline legislative alternatives. It can be used as a tool in the law-drafting process, but it does not present any recommendations for action or concrete proposals for national legislation on corporate social responsibility. Likewise, the extensive impact assessment to be carried out as part of the legislative work will have to wait until the official law-drafting process.

A number of studies on due diligence legislation have been published during the preparation of this report and more details of the progress of some the projects described in the report can be expected after its publication. Legislative projects and studies up to 31 May 2020 have been followed in this work.

1.2 Structure of the report

The objectives of the report are discussed in the first chapter, while the second chapter contains a brief description of the international regulation of human rights and the environment. This includes the Universal Declaration of Human Rights, international human rights and environmental conventions and the European Convention on Human Rights. The chapter describes the traditional division of responsibility between governments and businesses in human rights and environmental matters and examines how the due diligence obligation imposed on enterprises would change the situation. The concept and content of due diligence is described in the section of the second chapter reviewing the guidelines issued by the UN and the OECD. This description is necessary because many countries have also incorporated requirements on duties of care or on due diligence in their national legislation. An interview survey conducted with corporate representatives observed that different meanings are given to due diligence or duty of care. This observation probably arises from the fact that there are differences between the concepts used in the national legislation and case law.[13]

The third chapter discusses corporate social responsibility regulation at EU level. Key due diligence regulatory projects concerning such issues as non-financial reporting and regulation of high-risk sectors are presented in the chapter. National legislation on corporate social responsibility is discussed in the fourth chapter. The chapter discusses corporate social responsibility legislation in effect or under preparation in a number of

13 Study on Due Diligence, pp. 179–180, 59–61.

countries and such issues as the requirements for companies laid down in the legislation and their scope.

Chapter five examines different legal options for introducing corporate social responsibility legislation. We assess legislative solutions in corporate social responsibility legislation adopted in other countries, legislative proposals and a number of provisions incorporated in other areas of national legislation as a basis for a corporate due diligence law in Finland. The legislation on due diligence is examined from the perspective of enterprises, human rights and the environment.

The potential impacts of corporate social responsibility legislation and the issues that should be considered in the impact assessment are briefly discussed in chapter six.

The last chapter contains a summary and a tabular summary supporting it.

2 Regulatory environment

2.1 Introduction

2.1.1 Human rights

Human rights mean the universal, indivisible, inalienable and fundamental rights belonging to every individual. Human rights are enshrined in international and regional human rights instruments, which are binding agreements between states.

The current notion of human rights evolved in the aftermath of the Second World War. The Universal Declaration of Human Rights (1948) played a key role in this process. It lays down the most important internationally recognised human rights and defines the concept of human rights. Dozens of international human rights instruments have been adopted since the declaration. The International Covenant on Civil and Political Rights (1966) and the International Covenant on Economic, Social and Cultural Rights (1966) are among the most important. The European Convention of Human Rights (1950) and the conventions of the International Labour Organization (ILO) also play a key role. ILO sets out minimum standards universally for labour rights, supervises adherence to the conventions and supports member countries in complying with their provisions.[14] Supplementary instruments have been introduced to protect population groups in need of special protection. Their purpose is to safeguard the rights of such groups as women, children, people with disabilities, indigenous people, and migrant workers and their families.[15]

Human rights partially overlap with fundamental rights. For example, the right to life is both a human right and a fundamental right. However, fundamental rights also include rights that are not laid down in human rights conventions, such as the right to good

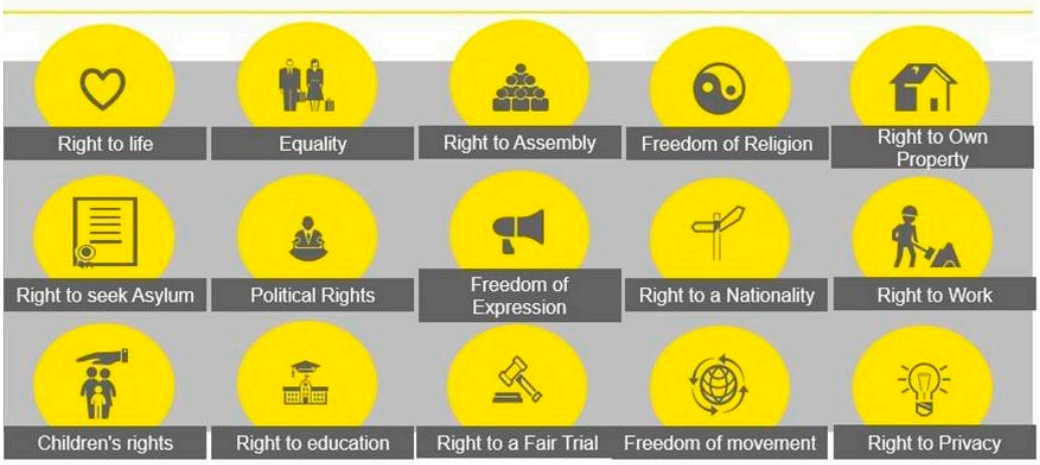
14 ILO website; How the ILO works

15 Convention on the Elimination of All Forms of Discrimination against Women (1979); Convention on the Rights of the Child (1989); International Convention on the Protection of the Rights of All Migrant Workers and Members of Their Families (1990); Convention on the Rights of Persons with Disabilities (2006); and the United Nations Declaration on the Rights of Indigenous Peoples (2007).

governance. At EU level, fundamental rights are enshrined in the Charter of Fundamental Rights of the European Union, which is part of the Union's binding primary law.[16]

International human rights treaties oblige countries to respect, protect, promote and fulfil human rights. The obligation to **respect** human rights means that countries may not act in a manner that interferes with or has an adverse impact on human rights. The obligation to **protect** human rights means that countries must protect individuals and groups against human rights violations. The obligation to **promote and fulfil** human rights means that countries must take positive action to facilitate the enjoyment of basic human rights.[17] In fact, the obligation of a country not to violate human rights is referred to as a negative obligation, while the obligation to promote them is referred to as a positive obligation. In practice, countries fulfil their obligations through legislation implementing the objectives of the treaties: to prevent human rights violations or to promote human rights.[18]

Human rights include:



*Examples of human rights defined in international treaties are listed above.

Finland has ratified the most important human rights treaties and it has harmonised its national legislation with the requirements laid down in them and in the Charter of Fundamental Rights of the European Union. The inviolability of human dignity and the freedom and rights of the individual are guaranteed in section 1 of the Constitution of Finland. Human rights are also listed in the second chapter of the Constitution, which lays down such fundamental rights as equality, the right to life and personal liberty and integrity, freedom of movement, protection of privacy, freedom of religion and

16 Website of the European Parliament: The protection of fundamental rights in the EU.

17 United Nations Human Rights Office of the High Commissioner: Frequently asked questions about the Guiding Principles of Business and Human Rights, 2014, p. 3.

18 See Heasman 2018, p. 40.

conscience, freedom of expression, freedom of assembly and association, protection of property, educational rights, the right to one's own language and culture, the right to work and freedom to engage in commercial activity. There are more detailed provisions on fundamental and human rights elsewhere in Finland's national legislation.[19] For example, provisions on the freedom of association are laid down in the Employment Contracts Act and the Criminal Code.[20]

2.1.2 The environment

Environmental law regulates the relationship of individuals with their environment. The legislation aims to control and minimise adverse impacts of human activities on the environment. Environmental rights are also often closely connected with human rights.[21] For example, the right to clean water is connected with both human rights and the protection of the environment. Environmental rights involve issues extending across generations. For example, safeguarding biodiversity and mitigating climate change concern future generations.[22] This thinking is also reflected in the goals of the UN 2030 Agenda for Sustainable Development.[23]

There are several international treaties and agreements regulating environmental rights. Finland is a party to more than one hundred environmental agreements that oblige countries, among other things, to reduce greenhouse gas emissions, to ensure environmental safety and health, and to preserve biodiversity.[24] Environmental protection in the EU is extensively harmonised by legislation, which aims to prevent environmental pollution, safeguard a healthy and pleasant environment, promote the sustainable use of natural resources and provide citizens with more opportunities to participate in decision-making.[25]

Under the Constitution of Finland, nature and its biodiversity, the environment and the national heritage are everyone's responsibility. The public authorities must endeavour

19 For example, the Non-Discrimination Act; Act on Equality between Women and Men (609/1986); Data Protection Act (1050/2018); Information Society Code (917/2014); Criminal Code; Act on the Freedom of Religion (453/2003); Act on the Exercise of Freedom of Expression in Mass Media (460/2003); Assembly Act (530/1999); Associations Act (503/1989); Employment Contracts Act; Language Act (423/2003); Freedom of Enterprise Act (122/1919).

20 Chapter 2, section 13 of the Constitution of Finland (731/1999); chapter 13, section 1 of the Employment Contracts Act (55/2001); chapter 47, section 5 of the Criminal Code (39/1889).

21 See *the Report of the Special Rapporteur on the issue of human rights obligations relating to the enjoyment of a safe, clean, healthy and sustainable environment,* A/HRC/37/59.

22 Ekroos et al. 2012, pp. 6–8.

23 2030 Agenda, see https://www.un.org/ga/search/view_doc.asp?symbol=A/RES/70/1&Lang=E.

24 See Ympäristöministeriö, *Kansainväliset ympäristösopimukset ja Suomi. Sopimukset kansainvälisen ympäristöyhteistyön edistäjinä*, Helsinki 2018 (available http://urn.fi/URN:ISBN:978-952-11-4810-1).

25 See chapter 1, section 1 of the Environmental Protection Act (527/2014).

to guarantee for everyone the right to a healthy environment and the opportunity to influence decisions that concern their own living environment.[26] More detailed provisions implementing these obligations are laid down in Finland's national environmental legislation.[27]

2.2 Guiding principles of the United Nations

In 2005, the United Nations appointed John Ruggie as the Special Representative of the Secretary-General on human rights and transnational corporations and other business enterprises. His mandate was to identify and to clarify what is expected of enterprises in the field of human rights.[28] In 2008, Ruggie presented the "protect, respect, remedy" framework built on three pillars: 1) the state duty to protect human rights; 2) the corporate responsibility to respect human rights; and 3) providing those affected with access to effective remedies.[29]

The UN Guiding Principles, adopted in 2011, are based on this framework.[30] The principles lay down the international standards for preventing and mitigating the adverse human rights impacts arising from business operations. The purpose of the UN Guiding Principles is not to substitute for legislation or to question the role of the state in the protection of human rights. However, enterprises should be aware how they respect human rights and demonstrate this in practice. The UN Guiding Principles also state that they should be implemented with particular attention to the rights of groups and individuals that may be particularly vulnerable.

First Pillar – the state duty to protect human rights

The state duty to protect human rights is laid down in the First Pillar of the UN Guiding Principles. This also includes the obligation to protect individuals against human rights abuses by business enterprises.

26 Section 20 of the Constitution of Finland.

27 For example, the Environmental Protection Act (527/2014); Nature Conservation Act (1096/1996); Water Act (587/2011); Act on Compensation for Environmental Damage (737/1994); and the Act on Environmental Impact Assessment Procedure (252/2017).

28 Commission on Human Rights, Human Rights and Transnational Corporations and Other Business Enterprises, E/CN.4/2005/L.87 (2005).

29 United Nations Human Rights Council, Protect, Respect and Remedy: a Framework for Business and Human Rights, 2008.

30 UN Guiding Principles: https://www.ohchr.org/Documents/Publications/GuidingPrinciplesBusinessHR_EN.pdf.

States must respect and protect the human rights of individuals within their territory and/or jurisdiction and ensure that individuals are able to enjoy their human rights. This means that states must protect individuals against human rights abuse by third parties, including business enterprises.[31] States must also set out clearly the expectation that all business enterprises domiciled in their territory and/or jurisdiction respect human rights in their operations.[32] States may be deemed to be in breach of their obligations if they fail to take appropriate steps to prevent, investigate, punish and redress abuse of human rights by private actors.[33] In practice, states fulfil their obligations through legislation applying to business enterprises.

Second Pillar – the corporate responsibility to respect human rights

The focus in the Second Pillar of the UN Guiding Principles is on corporate responsibility to respect human rights. Under the Guiding Principles, this means that business enterprises 'avoid causing or contributing to adverse human rights impacts through their own activities, and address such impacts when they occur'.[34] An 'adverse human rights impact' occurs when an action removes or reduces the ability of an individual to enjoy his or her human rights.[35] The responsibility of business enterprises to respect human rights applies to all enterprises regardless of for example their size, sector, ownership and structure.[36]

A business enterprise must introduce specific policies and processes to ensure respect for human rights. These include a policy commitment approved by the most senior level of the business enterprise, and which sets out the enterprise's human rights expectations.[37]

Business enterprises are also required to exercise human rights due diligence when working to ensure that their operations do not cause any adverse human rights impacts. Business enterprises should also have processes in place to remedy or to cooperation in remediation of the adverse human rights impacts that they have caused or to which they have contributed.

31 Principle 1 of the UN Guiding Principles.

32 Principle 2 of the UN Guiding Principles.

33 Principles 3–5 of the UN Guiding Principles.

34 Principle 13 of the UN Guiding Principles.

35 The Corporate Responsibility to Respect Human Rights – Interpretative Guide, 2012, p. 5.

36 Principle 14 of the UN Guiding Principles.

37 Principle 16 of the UN Guiding Principles.

Human rights due diligence laid out in the UN Guiding Principles requires:[38]

1. identification and assessment of actual and potential human rights and environmental impacts of the operations
2. prevention and mitigation of identified impacts and addressing of the impacts that have occurred
3. monitoring the effectiveness of the measures
4. providing information on the measures and their effectiveness.

Third Pillar – providing those affected with access to effective remedy

In the Third Pillar of the UN Guiding Principles, the focus is on the access to remedies or the chances of the individuals suffering from adverse human rights impacts to receive protection and compensation. Business enterprises are also partly responsible for the remedial action in this respect.[39] States must ensure that when human rights abuses occur within their jurisdiction those affected have access to effective remedy. The obligation covers setting up effective domestic judicial mechanisms to address adverse human rights impacts caused by business enterprises: it also should be ensured that procedural reasons, such as costs, do not constitute an obstacle to the submission of a claim.[40]

Business enterprises should establish mechanisms allowing grievances to be addressed early. Grievance mechanisms facilitate the identification of adverse human rights impacts and addressing of the impacts.[41] Both state and non-state grievance mechanism should ensure that individuals for whom the mechanisms are intended are aware of them, trust them and are able to use them. Similarly, an essential requirement is that the mechanisms are effective and easily accessible for the affected individuals.[42]

38 See Principles 17–22 of the UN Guiding Principles.

39 Principle 22 of the UN Guiding Principles.

40 Principles 25–26 of the UN Guiding Principles.

41 Principle 29 of the UN Guiding Principles.

42 Principle 31 of the UN Guiding Principles.

2.3 OECD Guidelines for Multinational Enterprises

The OECD Guidelines for Multinational Enterprises were first published in 1976. Since then, the document has been updated several times. For this report, the 2011 update is the most relevant: it added a new updated chapter on human rights and responsible supply chain management to the guidelines. The chapter on human rights is now consistent with the 'Protect, Respect and Remedy' framework of the United Nations. Due diligence and responsible supply chains are also discussed in more detail.[43] The OECD has also published a due diligence guidance document, in which due diligence processes are described in more detail.[44] The OECD guidelines combine all thematic areas of responsible business conduct, including human rights, employment and industrial relations, the environment, bribery, combating of bribe solicitation and extortion, consumer interests, science and technology, competition and taxation. The comprehensive approach makes the guidelines unique; they are the only document supported by governments that covers all major responsibility risks.

From the perspective of this report, the key difference between the OECD Guidelines and UN Guiding Principles is that in the first-mentioned, both human rights and the environment are covered. Under the guidelines, enterprises should, within the framework of laws, regulations and administrative practices in the countries in which they operate, and in consideration of relevant international agreements, principles, objectives, and standards, take due account of the need to protect the environment, public health and safety, and generally to conduct their activities in a manner contributing to the wider goal of sustainable development.[45]

The OECD Guidelines for Multinational Enterprises are recommendations addressed by governments to multinational enterprises. Even though the number of countries adhering to the guidelines is still relatively small (36 OECD member states and 12 countries outside the OECD), they account for a large proportion of the global economy, which adds to the weight of their commitment.[46] The guidelines provide non-binding principles and standards for responsible business conduct in a global context. The countries adhering to the guidelines are committed to promoting responsible business in accordance with applicable laws and internationally recognised standards.[47]

The guidelines are not a substitute for nor should they be considered to override domestic legislation.[48] However, in countries where domestic legislation conflicts with the principles

43 *OECD Guidelines for Multinational Enterprises 2011 Edition*, p. 3.

44 *OECD Due Diligence Guidance for Responsible Business Conduct,* 2018 (available http://mneguidelines.oecd.org/OECD-Due-Diligence-Guidance-for-Responsible-Business-Conduct.pdf).

45 OECD Guidelines for Multinational Enterprises, VI.

46 See OECD, *Perspectives on Global Development 2010. Shifting Wealth.*

47 OECD Guidelines for Multinational Enterprises, p. 3.

48 OECD Guidelines for Multinational Enterprises, p. 17.

and standards of the guidelines, enterprises should seek ways to honour such principles and standards to the fullest extent which does not place them in violation of domestic law.[49]

The OECD Guidelines for Multinational Enterprises set out a two-part obligation for governments: Firstly, they must promote responsible international business operations and encourage enterprises to contribute more extensively to economic, social and ecological development in global scale. Secondly, governments must establish National Contact Points, the purpose of which is to promote the application of the guidelines and to serve as discussion forums for applying the guidelines to individual cases. The Ministry of Economic Affairs and Employment, acting in collaboration with the Committee on Corporate Social Responsibility, acts as the National Contact Point for Finland.[50]

In 2018, the OECD issued the **Responsible Business Conduct** guidelines, which clarifies the content of the due diligence required of enterprises.[51]

2.4 Other UN initiatives

The purpose of the UN **Global Compact**, published in 2000, is to directly engage enterprises in human rights work. The tool is based on voluntary action and it does not provide governments with any official supervisory or enforcement role. Global Compact is based on ten principles. Participating companies must publish an annual progress report (Communication on Progress; COP) in which they restate their commitment to the principles and report on the practical measures they have taken and the results they have achieved.[52] In 2020, there were more than 10,000 enterprises from more than 160 countries participating in Global Compact.[53]

In 2014, the UN Human Rights Council established an inter-governmental working group to prepare a legally binding document on human rights in the operations of multinational enterprises and other companies.[54] The zero draft (2018) and the revised draft (2019) have already been circulated for comments.[55]

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49 OECD Guidelines for Multinational Enterprises, p. 17.

50 Handling Specific Instances of the OECD Guidelines for Multinational Enterprises.

51 OECD Due Diligence Guidance for Responsible Business Conduct, 2018 (available: http://mneguidelines.oecd.org/OECD-Due-Diligence-Guidance-for-Responsible-Business-Conduct.pdf).

52 See *UN Global Compact Policy on Communicating Progress* (https://d306pr3pise04h.cloudfront.net/docs/communication_on_progress%2FCOP_Policy.pdf)

53 https://www.unglobalcompact.org/.

54 UNHRC, Elaboration of an international legally binding instrument on transnational corporations and other business enterprises with respect to human rights, A/HRC/RES/26/9.

55 Zero draft, 16 July 2018; Revised draft, 16 July 2019.

3 Corporate social responsibility regulation in the European Union

3.1 Non-financial reporting

The financial statements, the management report and other reports prepared by a company are public documents and an important part of a company's annual reporting obligations.[56] To enhance the comparability of the information contained in financial statements, measures have been taken to harmonise regulation at EU level by requiring that EU-based listed companies prepare their consolidated financial statements in accordance with international standards (IFRS). By making reporting on responsibility measures a part of financial statements, legislation also obliges enterprises to provide investors and other stakeholders with comparable non-financial information.[57]

On 30 May 2001, the European Commission issued a recommendation on the recognition, measurement and disclosure of environmental issues in the annual accounts and annual reports of companies.[58] The recommendation was given because of the lack of clear reporting rules, which may have prompted investors, authorities, business analysts and other stakeholders to consider information disclosed by enterprises either inadequate or unreliable. In the absence of harmonised official reporting guidelines, it was also considered difficult to compare the reports of different companies. The purpose of the recommendation was to increase environmental reporting and enhance

56 Leppiniemi – Kykkänen 2019, pp. 18–19.

57 Communication from the Commission (2019/C 209/01) Guidelines on non-financial reporting: Supplement on reporting climate-related information, Section 1.1: "Without sufficient, reliable and comparable sustainability information provided by the investee companies, the financial sector cannot effectively direct capital towards investments that facilitate solutions to the sustainability crises ahead of us, nor can they effectively identify and manage the risks of investment that these crises pose."

58 C(2001) 1495 Commission Recommendation on the recognition, measurement and disclosure of environmental issues in the annual accounts and annual reports of companies (2001/453/EC).

its comparability.[59] The recommendation also encourages companies to publish environmental policies.[60]

Under the directive on non-financial information (NFI Directive),[61] adopted in 2014, large undertakings that are public-interest entities must provide a non-financial statement (NFI statement) containing the following:[62]

> "...information to the extent necessary for an understanding of the undertaking's development, performance, position and impact of its activity, relating to, as a minimum, environmental, social and employee matters, respect for human rights, anti-corruption and bribery matters, including:
>
> a. a brief description of the undertaking's business model.
> b. description of the policies pursued by the undertaking in relation to those matters, including due diligence processes implemented;
> c. the outcome of those policies;
> d. the principal risks related to those matters linked to the undertaking's operations including, where relevant and proportionate, its business relationships, products or services which are likely to cause adverse impacts in those areas, and how the undertaking manages those risks;
> e. non-financial key performance indicators relevant to the particular business."

When disclosing this information, undertakings may rely on national and international frameworks, including UN Guiding Principles and OECD Guidelines.[63]

The NFI Directive has been implemented in Finland by adding Chapter 3a to the Accounting Act. The reporting obligation applies to large public-interest entities with an average of 500 employees during the financial year. Thus, an enterprise must meet the criteria of a large undertaking and a public-interest entity laid down in accounting regulation. Under the Accounting Act and the Accounting Directive, a large undertaking is an enterprise exceeding at least two of the following three thresholds at the balance sheet date of the last completed financial year and the one immediately preceding it: 1) balance sheet total EUR 20 million; 2) net sales or corresponding revenue EUR 40 million; 3) an average of 250 employees during the financial year.[64] Listed companies, credit institutions

59 C(2001) 1495, paragraphs 4 and 5.

60 C (2001) 1495, paragraph 4: Disclosures.

61 Directive 2014/95/EU of the European Parliament and of the Council amending Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups.

62 Article 19a(1)1 of the NFI Directive.

63 Recital 9 of the NFI Directive.

64 Chapter 1, section 4 c of the Accounting Act (1336/1997), Article 3(4) of the Financial Statements Directive.

and insurance companies are considered as public-interest entities.[65] At EU level this definition applies to about 6,000 companies and in Finland to about 100 companies.[66]

The NFI statement can be included in the management report or submitted as a separate report, which must be published in connection with the management report or be posted on the company's website within a reasonable period of time (not exceeding six months after the balance sheet date).[67] The separate report must also be referred to in the management report.[68] If the company does not pursue policies in relation to one or more of these matters, the non-financial statement must provide a clear and reasoned explanation for not doing so.[69]

The Commission has supplemented regulation of non-financial reporting by issuing reporting guidelines,[70] which are intended to help companies report on information required under the directive in a high-quality and comparable manner. A supplement on reporting climate-related information has recently been added to the guidelines.[71] The reporting must cover both the impact of climate-related factors on the enterprise and the impacts of the enterprise's operations on climate.

In 2020, the European Commission launched a consultation on the need to amend the NFI Directive. The consultation was prompted by concerns related to the varying content and quality of NFI statements and the scope of the reporting obligation, which was considered insufficient in a number of respects.[72]

3.2 Due diligence in sector-specific regulation

The due diligence obligation varies between enterprises, sectors, products and regions and it is founded on risk-based assessment. Owing to higher risks related to specific sectors, raw materials and regions, the OECD has prepared sector-specific due diligence guidelines, which apply to extractive industries, clothing industries, agriculture, financing

65 Chapter 1, section 9 of the Accounting Act.

66 SWD(2019) 143, p. 20; TEM 57/2015, p. 7.

67 Provisions on the publication of the NFI statement by listed companies are laid down in Chapter 7, section 7 of the Securities Markets Act (746/2012) in the form of references to the Accounting Act.

68 Article 19a(4) of the NFI Directive.

69 Article 19a(1)2 of the NFI Directive.

70 European Commission, Guidelines on non-financial reporting (methodology for reporting non-financial information) (2017/C 215/01).

71 European Commission, Guidelines on non-financial reporting: Supplement on reporting climate-related information (2019/C 209/01).

72 See https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12129-Revision-of-Non-Financial-Reporting-Directive/public-consultation.

and minerals.[73] The EU has also considered it necessary to harmonise regulation applying to certain raw materials and sectors.

3.2.1 Timber

The EU regulation on obligations of operators placing timber and timber products on the market entered into force in 2013.[74] The Timber Regulation is part of the Action Plan on Forest Law Enforcement, Governance and Trade, (FLEGT 2003) launched by the EU in 2003 and prompted by the environmental, social and economic problems caused by illegal logging.[75] The regulation includes a due diligence obligation for operators to maintain a system that allows 1) access to information on timber placed on the market; 2) risk assessment; and 3) risk mitigation.[76]

Each operator must maintain and regularly evaluate the due diligence system which it uses, except where the operator makes use of a due diligence system established by a monitoring organisation referred to in Article 8 of the regulation.[77] Monitoring organisations can include, for example, organisations with expertise in the timber sector and legislative matters..[78] Competent authorities designated by Member States monitor the application of the regulation and they have the right to verify that operators comply with its provisions.[79] In Finland, the regulation and the provisions issued under it have been implemented by means of the Act on the Placing on the Market of Timber and Timber Products (897/2013; Timber Act). The Finnish Food Authority (formerly the Agency for Rural Affairs) has been designated as the competent Finnish authority.

3.2.2 Extractive industries

Under the Financial Statements Directive adopted in 2013,[80] large undertakings and public-interest entities active in the extractive industry or in the logging of primary forests must prepare and make public a report on payments made to governments on an annual

73 OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas; OECD paper on Responsible Business Conduct for Institutional Investors; OECD-FAO Guidance for Responsible Agricultural Supply Chains; OECD Due Diligence Guidance for Responsible Supply Chains in the Garment and Footwear Sector; OECD Recommendation on the OECD General Due Diligence Guidance for Responsible Business Conduct.

74 Regulation (EU) No 995/2010 of the European Parliament and of the Council laying down the obligations of operators who place timber and timber products on the market (Timber Regulation).

75 See COM(2003) 251, pp. 4–5.

76 Articles 4(2) and 6 of the Timber Regulation.

77 Article 4(3) of the Timber Regulation.

78 Recital 20 of the Timber Regulation.

79 Article 10 of the Timber Regulation.

80 Directive 2013/34/EU of the European Parliament and of the Council on the annual financial statements, consolidated financial statements and related reports of certain types (Financial Statements Directive).

basis.[81] The same obligation is also mentioned in the directive amending the Transparency Directive.[82] In Finland, the requirement has been implemented by means of separate legislation and by adding a disclosure obligation applying to listed companies to the Securities Markets Act.[83]

The obligation to report on payments was prompted by the close connection between corruption and illegal use of natural resources.[84] Reporting aims to help countries rich in natural resources implement the principles and criteria of EITI (Extractive Industries Transparency Initiative), which seeks to increase the transparency of the government revenue generated by the exploitation of natural resources.[85] The annual reporting obligation is country-specific and project-specific and it applies to payments in which a single payment or a series of related payments amounts to at least EUR 100,000.[86] Finnish companies within the scope of the Extractive Industries Act must submit their annual report for registration to the Finnish Patent and Registration Office in the same manner as their financial statements and management report.[87] A failure to prepare the yearly report and to submit it for registration constitute an offence under the law.[88]

3.2.3 Conflict minerals

The Conflict Minerals Regulation adopted in 2017[89] sets a due diligence obligation for certain operators importing minerals from conflict-affected and high-risk areas. Under this obligation the companies must: 1) adopt a supply chain policy and a management system; 2) assess the risk arising from their supply chains; 3) implement a risk-management plan; 4) carry audits via third parties; and 5) report on their operations on an annual basis. The regulation applies to the imports of tin, tantalum and tungsten, their ores, and gold, and aims to prevent armed groups and security forces from trading in these minerals. The

81 Article 42(1) of the Financial Statements Directive.

82 Directive 2013/50/EU of the European Parliament and of the Council amending Directive 2004/109/EC of the European Parliament and of the Council on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market, Directive 2003/71/EC of the European Parliament and of the Council on the prospectus to be published when securities are offered to the public or admitted to trading and Commission Directive 2007/14/EC laying down detailed rules for the implementation of certain provisions of Directive 2004/109/EC.

83 Act on the Disclosure of Fees paid to the Authorities by Companies engaged in Extractive Industries and Logging in Primeval Forests (1621/2015; Extractive Industries Act). Chapter 7, section 14 of the Securities Markets Act (746/2012).

84 COM(2003) 251, p. 4.

85 Recitals 44–45 of the Financial Statements Directive.

86 Section 5 of the Extractive Industries Act.

87 Section 8 of the Extractive Industries Act.

88 Section 9 of the Extractive Industries Act.

89 Regulation (EU) 2017/821 of the European Parliament and of the Council laying down supply chain due diligence obligations for Union importers of tin, tantalum and tungsten, their ores, and gold originating from conflict-affected and high-risk areas (Conflict Minerals Regulation).

regulation applies to parties importing minerals in excess of the volume thresholds laid down in the regulation. The regulation defines conflict-affected and high-risk areas as areas in a state of armed conflict or fragile post-conflict as well as areas witnessing weak or non-existent governance and security. These include failed states in which there are widespread and systematic violations of international law and human rights.[90] With regard to due diligence, the regulation refers to the due diligence guidelines of the OECD.[91]

Under the regulation, the Commission may adopt implementing acts laying down the list of global responsible smelters.[92] Independent third-party certifications may also be approved.[93] Authorities of the Member State are responsible for carrying out ex-post checks ensuring that operators within the scope of the regulation comply with the obligations laid down in the regulation.[94] Member States must establish the rules applicable to infringements of the regulation.[95] The due diligence obligation of the regulation will apply from 1 January 2021.[96] The Commission has also taken a number of measures to prepare for the implementation of the due diligence obligation.[97]

3.3 Other EU-level initiatives

3.3.1 Investors and investment products

The Shareholders' Rights Directive lays down provisions on listed companies to prepare a remuneration policy contributing to the business strategy, long-term interests and sustainability of the company. Under the directive, institutional investors and asset managers must also disclose their own engagement policy describing their investment strategy and the way in which they monitor the companies in relevant matters, such as social and environmental issues. The investors must also submit yearly reports on how the policy has been implemented.[98]

90 Article 2(1)f of the Conflict Minerals Regulation.

91 OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas (2013).

92 Article 9 of the Conflict Minerals Regulation.

93 Article 8 of the Conflict Minerals Regulation.

94 Article 11 of the Conflict Minerals Regulation.

95 Article 16 of the Conflict Minerals Regulation.

96 Article 20(3) of the Conflict Minerals Regulation.

97 SWD(2019) 143, pp. 22–23.

98 Directive (EU) 2017/828 of the European Parliament and of the Council amending Directive 2007/36/EC as regards the encouragement of long-term shareholder engagement.

As part of its action plan on sustainable finance, the European Union published a report on taxonomy regulation in March 2020.[99] Taxonomy is a classification system designed to create uniform criteria for determining whether an economic activity is environmentally sustainable. The classification system is intended to facilitate the transition to an economic system supporting the climate goals of the EU. Taxonomy lays out the criteria for sustainable development initiatives, which may concern 1) climate change mitigation; 2) climate change adaptation; 3) promoting the sustainable use and protection of water and marine resources; 4) promoting circulation economy and more effective waste prevention and recycling; 5) preventing and reducing environmental pollution; and 6) promoting the protection of healthy ecosystems.

To meet the requirements for taxonomy, an initiative must 1) substantially contribute to the achievement of at least one of the six environmental objectives listed above; 2) not significantly harm any of the other five environmental objectives; and 3) comply with minimum safeguards, which refer to, for example the UN Guiding Principles and the OECD Guidelines.[100] In this context, safeguards primarily mean processes helping to ensure that the initiative does not negatively impact other environmental objectives.

Provisions on the information to be disclosed are already included in the EU regulation on sustainability related disclosures in the financial services sector.[101] The purpose of the regulation is to increase the amount of available information on sustainability risks of investment products and to enhance and harmonise the content of the disclosures. The information provision obligation laid down in the regulation applies to financial market participants.[102] When assessing the impacts of investment decisions on sustainability factors, financial market participants should exercise due diligence in their risk-identification processes and report this on their websites.[103] The regulation will apply from 2021.

Quality of the information available to investors is also addressed in the regulation amending the EU benchmark regulation. The aim is to harmonise low-carbon benchmarks

99 EU Technical Expert Group on Sustainable Finance, *Taxonomy: Final Report of the Technical Expert Group on Sustainable Finance*, 2020.

100 EU Technical Expert Group on Sustainable Finance, T*axonomy: Final Report of the Technical Expert Group on Sustainable Finance*, 2020.

101 Regulation (EU) 2019/2088 of the European Parliament and of the Council on sustainability-related disclosures in the financial services sector.

102 Financial market participants are defined in Article 1 of the regulation.

103 Article 4(2)(d) of the EU regulation on sustainability-related disclosures in the financial services sector. With regard to standards, in recital 18 of the regulation there are references to the due diligence guidance for responsible business conduct developed by the OECD and the UN-supported Principles for Responsible Investment.

and enhance their quality and reliability by setting minimum requirements for the benchmarks.[104]

3.3.2 EU-level due diligence study

The **study on due diligence requirement throughout the supply chain** commissioned by the EU Commission was published in February 2020. The study examines European due diligence practices, legislation and opinions pertaining to human rights and the environment. With regard to possible EU-level regulation, the study identified the following options: 1) no EU-level regulation; 2) issuing new voluntary guidelines; 3) regulation on due diligence reporting; 4) introducing legislation on due diligence obligation. The study also contains a preliminary impact assessment of the options.[105] The study may provide a basis for EU-level regulation.[106]

3.3.3 European Green Deal

In December 2019, the European Commission presented the European Green Deal. The aim of the programme is to make the EU climate neutral by the year 2050. The programme sets out the European Green Deal investment plan and the just transition mechanism, which are designed to facilitate investments in climate neutrality and provide financial support for regions that are particularly hard hit by the economic impacts of the transition. The programme also includes a proposal for EU legislation designed to ensure that the EU will become climate neutral by the year 2050. In this way, a political commitment is intended to become legally binding on the Member States.[107]

The programme also contains a proposal for an European Climate Pact and communications on a European industrial strategy presenting a plan for a future European economy. Other proposals listed in the programme include (i) a proposal for a circular economy action plan focusing on the sustainable use of resources, (ii) From Farm to Fork strategy enhancing the sustainability of food supply chains; and (iii) the EU biodiversity strategy for 2030 designed to protect biodiversity.

104 Regulation (EU) 2019/2089 of the European Parliament and of the Council amending Regulation (EU) 2016/1011 as regards EU Climate Transition Benchmarks, EU Paris-aligned Benchmarks and sustainability-related disclosures for benchmarks.

105 The study and the annexes to it can be viewed at: https://op.europa.eu/s/n6eH.

106 See the speech by the EU Commissioner for Justice at the webinar in which the study was presented: https://responsiblebusinessconduct.eu/wp/2020/04/30/speech-by-commissioner-reynders-in-rbc-webinar-on-due-diligence/.

107 COM(2019) 640, European Green Deal; https://ec.europa.eu/info/strategy/priorities-2019-2024/european-green-deal_en.

4 Corporate social responsibility legislation in a number of countries

4.1 Adopted Legislation

4.1.1 United States

The California **Transparency in Supply Chains Act** (2010) is often considered as the first modern piece of corporate social responsibility legislation. The act entered into force on 1 January 2012, and it obliges retailers and manufacturers operating in the State of California to disclose the measures they apply to prevent the use of slavery and human trafficking in their supply chains. The obligation applies to enterprises with annual gross revenue of more than USD 100 million (about EUR 92 million).[108]

The disclosure must be posted on the company's website or sent to consumers on request. The disclosure must describe to what extent the company does the following: 1) verifies its supply chains to evaluate and address the risks of slavery and human trafficking; 2) conducts audits on its suppliers to evaluate supplier compliance with company standards for slavery and human trafficking in supply chains; 3) requires direct suppliers to certify that materials incorporated into the products comply with the local laws regarding slavery and human trafficking; 4) maintains internal accountability standards and procedures for employees or contractors failing to meet company standards regarding human trafficking; and 5) provides employees and managers responsible for the supply chain with training on slavery and human trafficking that is specifically designed to mitigate the risk arising from them.[109] As a consequence of a failure to disclose, a court may issue an injunction ordering the company to comply.[110]

108 United States, California, Transparency Act, Sec. 3(a).

109 United States, California, Transparency Act, Sec. 3(c).

110 United States, California, Transparency Act, Sec. 3(d).

The act has been criticised for not obliging companies to take any action to prevent human trafficking and for allowing companies to freely decide on the information they disclose. Companies can also meet their statutory reporting obligation by disclosing a report stating that no action has been taken. Studies concerning the act, show that most companies only meet the minimum disclosure requirements laid down in the act.[111] On the other hand, guidelines created as a result of the act and formulating best practices have been mentioned as positive effects of the act.[112]

The **Dodd-Franck Act** enacted in 2010 is another example of corporate social responsibility legislation introduced in the United States. Under the act, companies must disclose whether their conflict minerals originate from Congo and how the matter has been investigated. The companies must also provide information on products that are not conflict-free.[113] Under the act, companies must also provide reports on mine safety and the fees paid to the authorities by extractive industry companies.[114]

4.1.2 United Kingdom

The **Modern Slavery Act** (2015) of the United Kingdom contains a large number of provisions on human trafficking, slavery and forced labour.[115] The obligation of companies to disclose information laid down in the act is similar in its approach to the California Transparency Act. The act entered into force on 29 October 2015, and imposed a reporting obligation on UK-based companies with an annual net sales of at least GBP 36 million (about EUR 40 million).[116] Under the act, a company must publish an annual statement on the measures it has taken to ensure that there is no slavery or human trafficking in its supply chains or in its own operations. Alternatively, a company must publish a statement declaring that no action has been taken.[117] The net sales limit laid down in the act corresponds to the reporting limit laid down in the NFI Directive.[118] However, the scope of the act is wider than that of the directive as it also applies to other than public interest entities and it does not lay down requirements concerning the number of employees or the balance sheet.

111 Koekkoek et al. 2017, pp. 524–525.

112 Koekkoek et al. 2017, p. 526.

113 United States, section 1502 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act). See also Heasman 2018, pp. 138–142.

114 United States, sections 1503 and 1504 of the Dodd-Frank Act.

115 For example, Haynes 2016, s. 33–56.

116 United Kingdom, section 54(2)b of the Modern Slavery Act and Decree No. 1833, in which the net sales limit is set at GBP 36 million.

117 United Kingdom, section 54(4) of the Modern Slavery Act .

118 In the NFI Directive, the net sales limit of a large undertaking is set at EUR 40 million.

The focus in the statement is on supply chains. The company *may* disclose the following information: 1) organisational structure, business operations and supply chains; 2) company's policies in relation to slavery and human trafficking; 3) company's due diligence practices in relation to its business operations and supply chains; 4) the parts of the company's business and supply chains where there is a risk of slavery and human trafficking, and the steps that the company has taken to assess and manage that risk; 5) effectiveness of the company's risk-management procedures, as measured against suitable indicators; and 6) training in slavery and human trafficking issues available to the personnel.[119] Like the California **Transparency Act**, the **Modern Slavery Act** also allows companies to decide on the content of the statement. Thus, the content laid down in the act is only indicative. The act does not oblige companies to take any action against slavery or human trafficking as it concerns the obligation to investigate a company's actions. The act specifically also allows the company to submit a statement declaring that no action has been taken.

The Board of Directors or other equivalent decision-making body of the company must approve the statement and it must be published on the company website in an easily accessible form. If the company does not have a website, it must provide a copy of the statement within 30 days of the receipt of the request concerning the statement.[120] As in California, the failure to comply with the reporting obligation may prompt a court to issue an injunction ordering the company to fulfil the obligation. If the company still fails to comply with the obligation, a fine may be imposed on it.[121]

The reporting obligation only applies to companies operating in the United Kingdom. In a group of companies, the reporting obligation may only apply to the parent company operating in the United Kingdom or a subsidiary established in the United Kingdom. Such a group of companies may decide whether to publish more detailed statements concerning the entire group.[122]

An independent review of the **Modern Slavery Act** was published in 2019. The review noted that the objective of the act's disclosure obligation was to increase transparency and to level the playing field between companies that already operate in a responsible manner and companies that should improve their practices. Consumers, investors and non-governmental organisations were expected to assist in the monitoring of compliance with the obligation.[123] According to a preliminary assessment, the objectives of the act

119 United Kingdom, Modern Slavery Act 54(5)b.

120 United Kingdom, sections 54(6), 54(7) and 54(8) of the Modern Slavery Act.

121 United Kingdom, section 54(11) of the Modern Slavery Act; Home Office, *Transparency in Supply chains etc.: A practical guide,* Guidance issued under section 54(9) of the Modern Slavery Act 2015, p. 6.

122 Home Office, *Transparency in Supply Chains*, p. 8.

123 Home Office, *Transparency in Supply Chains, p. 6; Independent Review of the Modern Slavery Act* (2019), p. 39.

have not been met: it is estimated that up to one third of all companies have failed to fulfil their disclosure obligation. Absence of sanctions and supervision, and the ambiguities concerning the disclosure obligation were cited as reasons for this lack of compliance, as well as for the poor quality of the statements; especially the scope of the act has been considered vague.[124]

The fact that disclosure on the different areas of the statement is not mandatory and that there is an option of submitting a statement declaring that no action has been taken were also considered as problematic. The review suggested that reporting under different areas of the statement should be made mandatory and based on the comply or explain principle. The review also proposed that the content of the statements should be improved by means of guidelines. Moreover, it was recommended that the statement should be linked to the companies' other annual reporting obligations.[125] More centralised supervision of the reporting and more effective sanctions were also recommended.[126]

Under the **Bribery Act**, all companies based in the United Kingdom are obliged to act against bribery, irrespective of where they operate.[127] Companies may be held criminally liable for bribery taking place in connection with their operations. However, a company can be exonerated from liability if it can demonstrate that it had appropriate procedures in place to prevent bribery.[128] The Bribery act regulates a fairly limited sphere of activity. However, it has been proposed that some legislative solutions applied in it could also be used in human rights due diligence regulation.[129]

4.1.3 Australia

The Australian **Modern Slavery Act 2018** entered into force on 1 January 2019. In terms of its content, the reporting obligation laid down in the act is similar to that of the **Modern Slavery Act** of the United Kingdom. Under the act, companies established or operating in Australia with consolidated net sales of at least AUD 100 million (about EUR 60 million) per financial year must publish an annual statement on 'modern' slavery. The reporting obligation also applies to publicly owned companies,[130] and to about 3,000

124 *Independent Review of the Modern Slavery Act* (2019), p. 40.

125 *Independent Review of the Modern Slavery Act* (2019), pp. 41–42.

126 *Independent Review of the Modern Slavery Act* (2019), pp. 42–43.

127 United Kingdom, Bribery Act 2010.

128 *Insight into awareness and impact of the Bribery Act 2010*, pp. 6–7.

129 Pietropaoli et al. 2020.

130 Australia, Section 5(1) of the Modern Slavery Act 2018.

companies in total.[131] Companies whose net sales remains below the limit specified in the act may voluntarily comply with its requirements.[132]

The following matters must be described in the statement: 1) structure, business operations and supply chains of the company; 2) risks of modern slavery practices in the operations and supply chains of the company and the enterprises that it controls; 3) due diligence practices applied by the company in its business operations and supply chains; 4) action taken by the company and the enterprises that it controls to assess and manage risks (including due diligence); 5) the company's own estimate of the effectiveness of its risk-management measures; 6) the consultation process with the enterprises that the company controls; and 7) other matters considered relevant.[133] Unlike in the legislation adopted in California and the United Kingdom, the requirements laid down for the content of the statement are binding on the companies.

The Australian act also differs from its predecessors in terms of publication. The statements are submitted into a centralised register, which is publicly accessible. Before registration, the statements are checked to ensure compliance with the act's requirements.[134] If a company bound by the obligation fails to publish the statement, the responsible minister may demand that the company provides an explanation for its conduct or takes remedial action within 28 days.[135] If the company fails to provide an explanation for its conduct or does not take remedial action, the details of the company and the details of its non-compliance can be published in the register.[136]

The aim of the Australian act is to increase awareness and legal certainty, and to level the playing field among companies exceeding a specific net sales threshold. By introducing provisions on a centralised register and mandatory content of the statements, Australia explicitly sought to avoid the weaknesses of the act adopted in the United Kingdom, which mainly concern the quality and accessibility of the statements.[137] The reporting costs incurred by each company are put at about AUD 22,000 (about EUR 13,000).[138]

131 Commonwealth Modern Slavery Act, Guidance for Reporting Entities, p. 2.

132 Australia, Section 6(1) of the Modern Slavery Act 2018.

133 Australia, Section 16(1) of the Modern Slavery Act 2018.

134 Australia, Sections 18–19 of the Modern Slavery Act.

135 Australia, Section 16A(1) of the Modern Slavery Act 2018.

136 Australia, Section 16A(4)–(5) of the Modern Slavery Act 2018.

137 Department of Home Affairs, *Regulation Impact Statement. Modern Slavery Reporting Requirement,* p. 12.

138 Department of Home Affairs, *Regulation Impact Statement. Modern Slavery Reporting Requirement,* p. 14.

4.1.4 France

An act on corporate due diligence obligation was enacted in France in 2017.[139] A great deal of debate took place during the drafting stage and the act's final version can be considered a compromise. Under the act, large companies must exercise due diligence in human rights and environmental matters, and the obligation applies to the companies themselves and the enterprises that they control. The act applies to companies registered in France 1) with a workforce of at least 5,000 employees in the company itself or in its French-registered subsidiaries for two successive financial years; or 2) with a workforce of at least 10,000 employees in the company itself or in its subsidiaries registered in France or in other countries for a similar period.[140] It is estimated that the act applies to between 150 and 300 companies. However, the number of companies indirectly affected by the act is significantly higher.[141]

The due diligence obligation requires companies to prepare and implement a due diligence plan setting out measures that allow them to identify and prevent human rights violations and environmental damage directly or indirectly caused by their operations. The measures must apply to enterprises controlled by the company as well as its subcontractors and suppliers.[142] The plan should be prepared in cooperation with the company's stakeholders and it should cover the following: 1) identification, analysis and prioritisation of the risks; 2) regular evaluation of the operations of subsidiaries, subcontractors and suppliers; 3) measures to prevent adverse impacts; 4) a mechanism for collecting risk-related observations; and 5) a system for monitoring the implementation of the plan and its effectiveness.[143] The plan and the report on its implementation must be made publicly accessible as part of the company's annual reporting. The due diligence obligation laid down in the act can be considered to cover three areas: 1) preparation of the plan; 2) implementation of the plan; 3) publication of the plan and a report on its implementation.

Legal action can be taken against a company that fails to meet its due diligence obligation. The company is given three (3) months to meet its obligation on pain of a fine. Furthermore, a failure to comply with the obligations laid down in the act may result in liability for damages with respect to harm that could have been avoided if the company had fulfilled its statutory requirements. A court may also decide to make its decision public.[144] Liability for damages can only arise if there is damage, negligence in

139 France, La loi n°2017-399 relative au devoir de vigilance des sociétés mères et entreprises donneuses d'ordre.

140 France, Code du commerce, Article L. 225-102-4.-I. Of the scope of application, see also Brabant – Savorey 2017a, pp. 1–8.

141 Savorey 2020, p. 56.

142 France, Article L. 225-102-4. -I, par. 4.

143 France, Article L. 225-102-4. -I, par. 5.

144 France, Article L. 225-102-5. Savorey 2020, pp. 72–73.

regard to the obligations of the law and there is a causal link between them. The burden of proof lies with the party presenting the claim, which weakens the claimants chances of success, especially if the damage has occurred way down in the subcontracting and supply chain.[145] On the other hand, the chances of a company to exercise due diligence throughout long subcontracting chains may also be limited.[146]

4.1.5 The Netherlands

The Dutch act on due diligence obligation concerning child labour was approved in May 2019.[147] Originally, the act was intended to take effect on 1 January 2020, but its entry into force was since postponed. The exact date when the new act will become effective is not yet known.

Under the act, all companies selling products and services to Dutch end users must exercise due diligence in matters concerning the use of child labour.[148] The obligation applies to all companies irrespective of their size and country of establishment. Because the act applies to sales to end users it is not applicable to such operators as enterprises offering transport services.[149] The act also contains a provision, which allows granting sector-specific exemptions or exemptions based on the size of the company by general administrative order.[150]

Under the act, companies must pledge to exercise due diligence in matters concerning the use of child labour. The exact content of the pledge is not specified in the act. A company can also meet its obligation by giving a pledge of general nature. The pledge referred to in the act will be submitted to a supervisor, which will publish it in an electronic register.[151]

The due diligence obligation means that companies must check whether child labour is used in the supply of their products and services. The scope of the checks is restricted by stating that they must be based on sources that can be reasonably expected to be known and available to the company. This restriction also determines the level of due diligence. The content of due diligence is not specified in the act as it will be laid down by a general administrative order based on the ILO-IOE **Child Labour Guidance Tool for Business**

145 See Brabant – Savorey 2017b, Commentaires pp. 1–5.

146 See also commentary to Principle 17 of the UN Guiding Principles.

147 The Netherlands, Voorstel van wet van het lid Van Laar houdende de invoering van een zorgplicht ter voorkoming van de levering van goederen en diensten die met behulp van kinderarbeid tot stand zijn gekomen (Wet zorgplicht kinderarbeid).

148 The Netherlands, introduction; (https://zoek.officielebekendmakingen.nl/kst-34506-A.html).

149 The Netherlands, Art. 4(4).

150 The Netherlands, Art. 6. See Enneking 2020, p. 174.

151 The Netherlands, Art. 4.

report.[152] The act also allows preparation of joint action plans. Companies operating in compliance with such action plans are considered to exercise due diligence.[153]

If there is a possibility that child labour is used in the supply of products and services, the company must prepare and implement an action plan. A company is considered to exercise due diligence when it purchases products and services from companies that have pledged to exercise due diligence.[154]

Under the act, any natural or legal person whose interests have been affected by the failure of the company to exercise due diligence may submit a complaint to the supervisor. However, this right is narrowed by the requirement that there should be clear indications on non-compliance. Moreover, the supervisor can only consider the complaint after it has been submitted to the company in question and the company has not addressed the matter within a period of six (6) months in a satisfactory manner.[155] The supervisor may order the company to comply with the obligation to submit the pledge and to exercise due diligence, and impose an administrative fine on a company that has failed to comply with the order.[156] The maximum fine for failing to give the required pledge is EUR 8,200, and for failing to exercise due diligence EUR 820,000 (or 10% of the company's annual net sales).[157] Moreover, the company's management can be held criminally liable if the offence is repeated within five (5) years of the imposition of the administrative fine.[158]

The act does not contain any provisions under which victims of child labour could seek compensations. However, compensations can be sought under the principles of tort law.[159]

4.2 Planned legislation

4.2.1 Switzerland

In 2015, a citizens' initiative titled 'Responsible Business Initiative' was launched in Switzerland to introduce legislation obliging Swiss-based companies to exercise due diligence in human rights and environmental matters. Under the proposal, companies should respect human rights and the environment and ensure that the enterprises under

152 The Netherlands, Art. 5(3).
153 The Netherlands, Art. 5(4).
154 The Netherlands, Art. 5.
155 The Netherlands, Art. 3.
156 The Netherlands, Art. 7.
157 Enneking 2020, p. 177.
158 The Netherlands, Art. 9.
159 Enneking 2020, pp. 177–178.

their control also meet this requirement. The act would also oblige companies to exercise due diligence in all business relationships. Moreover, companies would be liable for damages for human rights and environmental violations occurring in their operations. In order to avoid liability, companies would have to demonstrate that they have exercised due diligence. Under the act, Swiss law could also be applied in situations in which the legislation of other countries would normally apply.[160]

The proposal was rejected by the Swiss Parliament. However, the lower chamber of the Parliament presented its own counter-proposal in May 2018.[161] Under the counter-proposal, the obligation would apply to companies meeting **at least two** of the following requirements during two successive financial years: 1) the balance sheet total is at least CHF 40 million (about EUR 38 million); 2) the sales total at least CHF 80 million (about EUR 75 million); and 3) the average number of employees is at least 500.[162] The economic thresholds are set higher that in the NFI Directive.[163] However, there would be one exception to the application of the thresholds: the due diligence obligation would apply to companies that do not exceed the thresholds but whose activities entail a particularly high risk of violating provisions on the protection of human rights and the environment. At the same time, the obligation would not apply to companies operating with a particularly low risk. Separate provisions would be laid down on the risk assessment procedure.[164]

Under the counter-proposal, the due diligence obligation would apply to the company's board of directors, which would also be responsible for the due diligence risk assessment, mitigation of the impacts, ensuring access to remedial measures, and monitoring the effectiveness of the measures. Companies would also be obliged to publish a report on adhering to the obligation.[165] Like the original proposal, the counter-proposal would also make a parent company liable for damage caused by companies under its control. However, it is stated in the counter-proposal that the control does not arise on the grounds that a company is financially dependent on another company. Thus, liability for damages would not apply to damages caused by a subcontractor that is financially dependent on the company. Under the proposal, compensation would only be provided for personal injury and property damage. Furthermore, the liability for damages set

160 The official language versions of the proposal can be viewed at https://www.bk.admin.ch/ch/f/pore/vi/vis462t.html and the unofficial English translation at https://corporatejustice.ch/wp-content/uploads//2018/06/KVI_Factsheet_5_E.pdf.

161 Swiss Parliament counter-proposal (unofficial translation).

162 The proposed change would be implemented by means of additions to the Code of Obligations regulating agreements and companies. See Article 716a^{bis}(3).

163 In addition to having an average workforce of 500, large public-interest companies would also have to post a balance sheet of at least EUR 20 million or net sales of at least EUR 40 million.

164 Switzerland, Code of Obligations, Art. 716a^{bis}(4). See also Bueno 2018.

165 Switzerland, Code of Obligations, Art. 961e.

out in the counter-proposal would specifically apply to the company and not to its management.[166] The conflict of laws provision under which Swiss law could apply to situations in which the legislation of other countries would normally apply is also contained in the counter-proposal.[167]

The upper chamber of the Swiss Parliament rejected the counter-proposal and presented its own proposal (which was supported by the Swiss Government) in December 2019. The reporting obligation and the due diligence obligation concerning the imports of conflict minerals are contained in this proposal.[168] The lower chamber of the Parliament has stuck to its counter-proposal and the final form of the legislation remains open.

4.2.2 Germany

In Germany, there is debate on corporate social responsibility on many fronts. At the end of 2016, the German government adopted a national action plan on companies and human rights (Nationale Aktionsplan Wirtschaft und Menschenrechte, *NAP*). The purpose of the action plan is to ensure that companies exercise due diligence in human rights matters and thus implement the goals set out in the 2030 Agenda for Sustainable Development. The German government monitors the achievement of the goals on an annual basis. The aim is that at least half of all companies with more than 500 employees would incorporate human rights due diligence in their processes by the year 2020. Decisions on further measures will be taken on the basis of the achievement of the goal and they may include legislative action.[169]

A draft law on sustainable value chains (Nachhaltige Wertschöpfungskettengesetz – NaWKG) prepared by the Federal Ministry for Economic Cooperation and Development (Bundesministerium für wirtschaftliche Zusammenarbeit und Entwicklung) was leaked to the public in 2019. The proposal contains a due diligence obligation.[170] The leaked proposal does not have any official status and it is not supported by other ministries. The proposal may, however, be taken up again if voluntary measures do not produce the desired results.

166 Switzerland, Code of Obligations, Art. 55, Art. 759a, Art. 981a.

167 Switzerland, Federal Act on Private International Law, Art. 139a.

168 The proposal presented by the Conseil des Etats can be viewed at: https://www.parlament.ch/centers/eparl/curia/2016/20160077/S2-44%20F.pdf.

169 https://www.csr-in-deutschland.de/EN/Business-Human-Rights/business-human-rights.html. See also Augenstein, 2020, p. 112.

170 The German text can be viewed at: https://www.business-humanrights.org/sites/default/files/documents/SorgfaltGesetzentwurf_0.pdf; an unofficial English translation can be viewed at: https://die-korrespondenten.de/fileadmin/user_upload/die-korrespondenten.de/DueDiligenceLawGermany.pdf. See also Augenstein, 2020, p. 113.

The purpose of the proposed act would be to safeguard human rights and the environment in international value chains.[171] The act would apply to large German-based companies and companies that operate themselves or through companies that they control in high-risk sectors or conflict regions.[172] The act would also apply to foreign operations of these companies but it would not apply to small enterprises.[173] The thresholds for large companies laid down in the Accounting Directive would be used. Thus, the act would apply to companies that exceed at least two of the following thresholds during two successive financial years: 1) balance sheet total EUR 20 million; 2) net sales EUR 40 million; and 3) an average of 250 employees.[174]

The companies within the scope of the act should exercise due diligence to protect all internationally recognised human rights[175], to protect the environment and to avoid environmental damage. The required level of environmental protection is defined in local legislation and the international agreements binding on Germany.[176]

Due diligence would comprise the following parts: 1) The company should prepare a risk analysis of its operations and update it on a continuous basis. The extent of the risk analysis would depend on the sector and operating area of the company and the focus should be on recognised risks. The analysis should cover the entire value chain of the company, including its subcontractors, products and services.[177] 2) The company should take the required measures to prevent recognised risks and to take action to mitigate the effects.[178] 3) The company should appoint a compliance officer who is responsible for compliance with the due diligence obligation and reports to the company's management. The compliance officer should also be heard before any strategic business decisions are taken.[179] 4) The company should establish an internal complaints mechanism and ensure the protection of whistle-blowers.[180] 5) The company should also document its due diligence practices and publish a report on the action taken.[181]

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171 Germany, section 1 of NaWKG.

172 The following sectors are listed in section 3(6) of the NaWKG. The following sectors are listed as high-risk sectors in the act: 1) agriculture, forestry and fisheries; 2) mining and quarrying; 3) manufacture of food products; 4) manufacture of textiles; 5) manufacture of clothing; 6) manufacture of leather goods and footwear; 7) manufacture of computers and electronic and optical products; and 8) electric, gas, heating and air conditioning maintenance.

173 Germany, Section 2 of NaWKG.

174 Section 3(3) of NaWKG refers to the definition of a large company in section 267 of the German trade act (Handelsgesetzbuch).

175 See Germany, Annex 1 to NaWKG, which lists the international human rights conventions referred to in the act.

176 Germany, sections 3(8) and 4 of NaWKG.

177 Germany, section 5 of NaWKG.

178 Germany, sections 6 and 7 of NaWKG.

179 Germany, section 8 of NaWKG.

180 Germany, sections 9 and 10 of NaWKG.

181 Germany, section 11 of NaWKG.

Supervising compliance with the act would be the responsibility of a competent authority, which would have the right to conduct inspections in the company's premises and request information from the company. Administrative fines of up to five million euros could be imposed on a company failing to exercise due diligence.[182] A company receiving fines of at least EUR 250,000 could also be excluded from the award of public contracts.[183] The compliance officer would also be criminally liable for his/her actions.[184]

4.2.3 Nordic countries

In Norway, a government-appointed committee submitted a report in November 2019 proposing legislation on corporate social responsibility and supply chains. Under the proposal, companies would be obligated to be aware of the key adverse impacts of their operations and supply chains on human rights. The extent of the obligation would depend on such matters as the size and operations of the company. The obligation would always apply to the most serious human rights risks, such as the use of child and slave labour. Companies selling consumer products would also have to disclose information of their production sites.

Under the Norwegian legislative draft, companies would also be obliged to answer questions concerning their human rights actions. Under the legislative draft, large companies[185] would also be obliged to exercise due diligence with regard to the human rights impacts of their operations and to publicly report on them and their due diligence measures. The Norwegian consumer protection authority would be responsible for supervising compliance with the act and it could also impose fines for failure to adhere to its obligations.[186]

In Denmark a proposal for a human rights due diligence obligation for companies was also introduced. The proposal has not, however, made any progress in the Danish Parliament.[187]

182 Germany, Section 13 of NaWKG.

183 Germany, Section 16 of NaWKG.

184 Germany, Section 14 of NaWKG.

185 A large company is an enterprise exceeding at least two of the following thresholds: balance sheet NOK 35 million (about EUR 3.25 million); net sales NOK 70 million (about EUR 6.5 million); and at least 50 employees.

186 See Mestad et al. 2019 (available: https://www.regjeringen.no/contentassets/6b4a42400f3341958e0b62d40f484371/ethics-information-committee---part-i.pdf).

187 For details of the Danish proposal, visit: https://www.ft.dk/samling/20181/beslutningsforslag/B82/bilag.htm.

5 Implementing a national due diligence obligation – legal analysis

5.1 Purpose of the legislation and regulatory options

5.1.1 Objective of due diligence

The purpose of the envisaged act examined in this report would be to impose a human rights and environmental due diligence obligation on companies. Under the UN Guiding Principles, all companies must exercise due diligence irrespective of where they operate.[188] The OECD Guidelines are intended for multinational companies. Both documents have their foundations in the observation that globalisation has given rise to regulatory gaps, and that there is a need to regulate transboundary operations of multinational companies in areas where legislation or legislative controls do not adequately protect human rights and the environment.[189]

A statutory due diligence obligation would transform practices described in non-binding soft law instruments, UN Guiding Principles and the OECD Guidelines into binding provisions and impose new obligations on companies, especially in areas where the legislation protecting human rights and the environment or its enforcement are not well-developed. In Finland, companies would be required to consider human rights and the environment in their operations.

Implementing a due diligence obligation does not intend to change national human rights and environmental legislation or to interfere with the requirements laid down in them. The due diligence required under the act would not be a substitute for duties of care or impact assessments required elsewhere in the law (for example, in the

188 Commentary to Principle 11 of the UN Guiding Principles.

189 Ruggie, John, Protect, *Respect and Remedy: a Framework for Business and Human Rights,* A/HRC/8/5 (https://www.undocs.org/A/HRC/8/5), sections 3, 14, 16; Salminen – Rajavuori 2019, p. 387. The focus in the Study on Due Diligence prepared by the European Commission is also on due diligence in companies' supply chains.

environmental legislation).[190] This aspect could be highlighted, for example, by including in the envisaged act a section that clarifies the relationship between the due diligence obligation and other legislation. Moreover, to prevent any interpretative ambiguities, the objective of the legislation and its scope could be clarified by stating the key objective or purpose of the act in a separate section at the start of the act.[191] For example, protecting human rights and the environment in global value chains is set as the objective of the unofficial German legislative draft.[192]

National legislation contains obligations concerning human rights and the environment. The relationship between a new due diligence obligation concerning human rights and the environment and the rest of the legislation could be clarified in a separate section. To prevent any interpretative ambiguities, the objective of the legislation and its scope could also be clarified in a section at the start of the act.

5.1.2 Regulatory options

Corporate social responsibility concerning human rights and the environment can be promoted by applying a range of different regulatory solutions. The following options were reviewed in the Study on Due Diligence (2020), a report discussing regulation at EU level: 1) no policy change; 2) new voluntary guidelines/guidance; 3) new regulation requiring due diligence reporting; or 4) new regulation requiring mandatory due diligence as a legal duty of care.[193]

Non-binding voluntary guidelines have played an important role in the development of responsible business operations. In addition to non-binding guidelines, binding legislation has also been adopted. There are two main approaches to national due diligence legislation: 1) introducing a reporting obligation (California, United Kingdom and Australia); or 2) introducing a due diligence obligation (France and the Netherlands and the legislative proposals in Germany and Switzerland). Both approaches have also been used in EU legislation: Large public-interest entities are required to disclose non-financial

190 In the review produced in the United Kingdom, it was considered appropriate to examine environmental due diligence as part of human rights because the environment is already extensively protected (partially on the basis of strict liability) and the view was that the due diligence obligation might narrow the scope of this protection; Pietropaoli et al. 2020, p. 28 footnote 73.

191 See Lainkirjoittajan opas, 18.1; http://lainkirjoittaja.finlex.fi/18-lain-ja-asetuksen-alkusaannokset/18-1/.

192 Germany, Section 1 of NaWKG.

193 See Study on Due Diligence, pp. 239–259.

information in their annual reports,[194] and a due diligence obligation applies to the imports of conflict minerals and timber.[195]

These two approaches are not mutually exclusive. All legislation imposing a due diligence obligation also require reporting. As additional options, companies could also be encouraged to act in a responsible manner by requiring due diligence in state-funded projects or by offering financing on more favourable conditions to responsible companies.[196] Changes in legislation could also be made incrementally, for example, by gradually increasing a company's obligations and/or their supervision as more information on the implementation of the already imposed obligations becomes available.[197]

In this report, the focus is on assessing the due diligence obligation imposed on companies. The reporting obligation is examined as one of the obligations that could be introduced as part of due diligence. The option of making no legislative changes should be considered in the national legislative process but is not treated in this report. Similarly, voluntary guidelines are not discussed in this report as an independent alternative. Rather they are primarily considered as an element supplementing any corporate social responsibility legislation.

5.2 Due diligence as a legal obligation

5.2.1 Due diligence in non-binding principles

Under the UN Guiding Principles, due diligence[198] involves a process aimed at preventing adverse human rights impacts arising from companies' operations. The process should be ongoing, and its content varies depending on the nature and complexity of the company's operations. Companies exercising due diligence should:

194 NFI Directive.

195 Conflict Minerals Regulation; Timber Regulation.

196 The UN Guiding Principles (commentary to Principle 3) call for countries to consider a smart mix of measures that include voluntary and mandatory measures at national and international level. See also De Schutter et al. 2012, pp. 4–5.

197 It was proposed in the memorandum reviewing the Modern Slavery Act of the United Kingdom that the adjustment of companies should be facilitated by gradually introducing harsher sanctions for failure to comply with the statutory reporting obligation; Independent Review of the Modern Slavery Act 2015, p. 46. Of the same approach in the French legislation, see Savorey 2020, pp. 78–79.

198 In the Finnish operating environment, the English term due diligence appears mainly describing the review preceding a corporate acquisition. There are some indications of more extensive use of the term 'due diligence' in Finnish legislation. The term is used, for example, in the Finnish version of the Conflict Minerals Regulation. The concept 'duty of care' (fin. huolellisuus) is, however, more commonly used in national legislation. The requirement that general language should be used in legislative texts favours using the familiar concept of duty of care in legislation; see Lainkirjoittajan opas, 24.2.1 (http://lainkirjoittaja.finlex.fi/). Of the use of the terms 'care' and 'due diligence' see also Bonnitcha – McCorquodale 2017.

1. **identify and assess** any actual or potential adverse human rights impacts with which they may be involved either through their own activities or as a result of their business relationships.[199]
2. **prevent and mitigate** adverse human rights impacts that they have identified.[200]
3. **track** the effectiveness of their response to verify whether adverse human rights impacts are being addressed.[201]
4. **communicate** how they have addressed the human rights impacts of their operations.[202]

Providing remediation for adverse impacts arising from a company's operations is a part of the prevention and mitigation of the impacts. Where business enterprises identify that they have caused or contributed to adverse impacts, they should provide for or cooperate in their remediation.[203]

The Office of the United Nations High Commissioner for Human Rights defines due diligence as "such a measure of prudence, activity, or assiduity, as is properly to be expected from, and ordinarily exercised by, a reasonable and prudent [person] under the particular circumstances".[204] The requirement of reasonability specifies the content of due diligence and refers to a context-specific and risk-based approach. The content and measures of exercising due diligence are not measured by uniform standards. Appropriate due diligence measures depend on such factors as the business sector concerned, the company's size, structure and geographical area of operations and other risk factors. Likewise, assessing compliance with due diligence is done on a case-by-case basis.[205] For example, due diligence required when planning to build a factory in a non-EEA country and the associated processes differ substantially from the due diligence and processes that can be expected of a SME planning to sell its products through a branch in a European country.

199 Principle 18 of the UN Guiding Principles.

200 Principle 19 of the UN Guiding Principles.

201 Principle 20 of the UN Guiding Principles

202 Principle 21 of the UN Guiding Principles.

203 Principle 22 of the UN Guiding Principles.

204 The Corporate Responsibility to Respect Human Rights – Interpretative Guide, 2012, p. 6.

205 UN Guiding Principles, Principle 17, Section b; The Corporate Responsibility to Respect Human Rights – Interpretative Guide, 2012, pp. 5 and 27.

The content of the due diligence set out in the UN Guiding Principles and the OECD Guidelines can be summed up as follows:[206]

- Due diligence comprises different processes;
- Due diligence is preventive in nature;
- Due diligence is context-specific and risk-based (priority should be on the most serious risks);
- Due diligence is an ongoing process.

Companies exercising due diligence should 1) identify and assess the impacts of their operations on human rights and the environment; 2) prevent and mitigate identified adverse impacts, 3) monitor the effectiveness of their actions; and 4) disseminate information on them. The qualifier 'due' preceding the term 'diligence' means that different companies can apply it in different ways.

Due diligence is a risk-based process. Companies should identify and prioritise the most significant risks to human rights and the environment arising from their operations.

5.2.2 Duty of care and due diligence in legislation

The term 'due diligence' used in the UN Guiding Principles and the OECD Guidelines has in the Finnish versions of the texts been translated using the term 'duty of care' (*huolellisuusvelvoite or asianmukainen huolellisuus*). As due diligence describe by the UN Guiding Principles and the OECD Guidelines could be framed as duty of care in legislation, these terms are used interchangeably in this report.

The due diligence requirement discussed in this report is similar to duty of care requirements found in a number of laws in Finland. The content and extent of a duty of care can vary.[207] However, in general, a duty of care means the obligation to act in order to prevent specific risks from being realised. Duty of care, like due diligence, does not oblige the parties concerned to achieve a specific end result. Thus, the realisation of operational risks does not automatically mean that the actor had failed to exercise its duty of care.[208] The second key feature of a duty of care and due diligence obligation is that an actor may defend itself against legal liability by showing it has taken measures required in the circumstances. The due diligence exercised by the actor is assessed objectively and in a

206 See Study on Due Diligence, pp. 159–160.

207 Heasman 2020; Study on Due Diligence, pp. 250–251.

208 Of the general obligation to exercise care, see also Study on Due Diligence, p. 158.

context-specific manner, compared with the way in which an individual exercising care would act in a similar situation.

One example of a national duty of care requirement is found in the Environmental Protection Act, which requires operators to have knowledge of the environmental impacts and risks of their operations, and to organise their operations in such a way that environmental pollution can be prevented in advance. Where pollution cannot be fully prevented, it must be limited to the lowest level possible.[209]

Similarly, the management of a limited liability company is required to act with due care and promote the interests of the company (duty of care).[210] The duty of care means that the company management must base its business decisions on due care and accurate information.[211] The requirement to exercise due care is assessed objectively and compared with the way in which an individual exercising due care would act in a similar situation. The assessment is based on the situation at the time of the decision-making. Risks and risk-taking are inherent in business operations and assessing them is part of decision-making. Realisation of the risk (a business decision proves a failure) does not automatically mean that the management has failed to exercise due care.[212] When a decision involves significant risks, more information must also be obtained before the decision is made.[213] There are also many other Finnish pieces of legislation containing provisions on the duty of care.[214]

The company's management is responsible for ensuring that the company complies with applicable regulatory provisions. Companies operating in Finland and their management must meet a broad range of different requirements concerning due care relating to risks. The content and scope of the requirements are context-specific and on a case-by-case basis. As a rule, the obligations to exercise care are only briefly described. One exception

209 Sections 6 and 7 of the Environmental Protection Act. Under the OECD Guidelines (VI.69) preventive action must be taken as early as possible.

210 Chapter 1, section 8 of the Limited Liability Companies Act. Similar provisions on the duty of care are also contained in other Finnish pieces of legislation on corporations and associations; Chapter 1, section 8 of the Cooperatives Act (421/2013); Chapter 1, section 23 of the Insurance Companies Act; Chapter 6, section 35 of the Associations Act (503/1989); and Chapter 1, section 4 of the Foundations Act (487/2015). A similar obligation also applies to estate administrators in insolvencies; Chapter 14, section 3 of the Bankruptcy Act (120/2004).

211 HE 109/2005 vp., p. 195.

212 HE 109/2005 vp., p. 195.

213 Airaksinen et al. 2018, pp. 50–55; Mähönen – Villa 2015, pp. 365–383.

214 Below are some of the pieces of legislation containing the obligation to exercise care: Chapter 2, section 4 of the Rescue Act (379/2011); Chapter 2, section 5 of the Consumer Safety Act (920/2011); Chapter 3, section 16 of the Food Act (23/2006); sections 32 and 54 of the Lift Safety Act (1134/2016); section 21 of the Electrical Safety Act (1135/2016); and Chapter 4, section 19 of the Chemicals Act (599/2013).

is the Occupational Safety and Health Act, in which several subsections are devoted to the employer's obligations and the factors that should be considered in them.[215]

Acting with care typically involves obtaining of the required information, risk-based assessment, prevention of risks and continuous monitoring. In fact, care referred to in national legislation contains the same elements as the due diligence described in the UN Guiding Principles and the OECD Guidelines. The due diligence obligation concerning human rights and the environment can thus be formulated as a general objective to promote specific goals or to prevent specific risks.

In practice, companies assess the risks connected with their operations on a continuous basis, work to prevent them, monitor their performance and provide information on their operations. In due diligence legislation, the focus in risk assessment is on the risks to human rights and the environment arising from the company's operations. Thus, the approach differs from the approach in which risks are assessed from the company's perspective.[216] Even though human rights and environmental risks may also manifest as business risks (for example, by damaging the company's reputation), companies must take a different approach to the management of risks when exercising human rights and environmental due diligence.[217]

In legislation, duty of care usually refers to the obligation to exercise appropriate care in order to prevent specific risks. Duty of care or due diligence in human rights and environmental matters would mean that companies must take measures to prevent human rights and environmental risks arising from their operations.

Duty of care and due diligence are context-specific and actions that operators are required to take may vary. Due diligence does not oblige the parties concerned to achieve a specific end result. Thus, the realisation of operational risks does not automatically mean that the obligation to exercise due care had been neglected. The assessment of whether the actor exercised required care is carried out retrospectively on an objective basis.

215 Chapter 2, section 8 of the Occupational Safety and Health Act (738/2002). The obligation covers the assessment of occupational safety and health factors, which should be in accordance with the principle of proportionality, prevention and elimination of hazards and risk factors, and continuous monitoring. If necessary, outside experts must be used in the assessment (Chapter 2, section 10). The case-specific assessment of the appropriateness and proportionality of the duty of care has also been discussed in case law; KKO 2014:75; KKO 2016:99.

216 Study on Due Diligence, p. 222.

217 In its guidelines on climate-related reporting required under the NFI Directive, the European Commission draws attention to differences between environmental risk perspectives and to the differences between factors impacting the value of the company and factors influencing its operating environment and society at large. According to the guidelines, companies should also pay attention to the different time spans of the approaches: "When assessing the materiality of climate-related information, companies should consider a longer-term time horizon than is traditionally the case for financial information"; Communication from the Commission, Guidelines on non-financial reporting:— Supplement on reporting climate-related information (2019/C 209/01), 2.2.

5.2.3 Process of due diligence

As a rule, companies are free to decide how to organise their risk-assessment and risk-prevention procedures in the most suitable and optimum manner. The purpose of the due diligence obligation is to encourage companies to introduce adequate measures and processes to ensure care. These measures and processes can be defined in the law or left to be assessed on a case-by-case basis. In practice, companies identify and manage their adverse human rights and environmental impacts, for example, by means of risk assessments, contractual terms, and supplier audits, and by requiring suppliers to carry out self-evaluations. A range of different management systems can be used in the assessment of human rights and environmental impacts or the company can incorporate the processes into its existing risk assessment procedures.[218] In legislation, companies can be obliged to introduce at least some of these measures.[219]

5.2.3.1 Identifying the impacts

The purpose of due diligence defined in the UN Guiding Principles is to prevent adverse impacts of business operations. The adverse impacts can only be prevented if the (potential) impacts of the operations can be identified.

Companies could be obliged to meet a duty to know (similar to that laid down in the Environmental Protection Act), which would apply to the human rights and environmental impacts of their operations.[220] A similar human rights obligation is proposed in the Norwegian report.[221] The duty to know would not mean that the operator must be aware of all impacts of its operations as it usually includes an element of proportionality and appropriateness.[222] The content of the obligation would vary, depending on such matters as the sector and operating area of the company.[223] According to the UN Guiding Principles companies should identify the risks that are the most severe and prioritise their action so that they can prevent and mitigate such risks.[224] For example, companies with long supply chains may give priority to the parts of the supply chain with the highest risk and focus their efforts on them.[225]

218 Commentary to Principle 17 of the UN Guiding Principles.

219 Examples of provisions on internal company control can be found in such pieces of legislation as the Act on Credit Institutions; Chapter 7 of the act lays down requirements for management and control systems.

220 Chapter 2, section 6 of the Environmental Protection Act.

221 Norway, Sec. 5.

222 See KHO 2014:187. For the Norwegian draft, see Mestad et al. 2019, p. 65.

223 Klinger et al. 2016, p. 26.

224 Principle 24 of the UN Guiding Principles.

225 OECD Guidelines, Commentary on General Policies, section 16.

The unofficial legislative proposal presented in Germany includes a provision on the factors to be considered when carrying out risk analysis, and a provision on integrating preventive measures into the company's business processes.[226] In legislation, identification and prioritisation of essential risks by the company could be steered, for example, by obliging companies to pay particular attention to highly vulnerable groups. Instead of a duty to know, the proportionality of the obligation could also be underlined by introducing a statutory obligation to identify or assess the human rights and environmental risks arising from the company's operations.

Under the UN Guiding Principles, companies should establish or participate in grievance mechanisms allowing companies' stakeholders to report to the company on risks or impacts that have already been realised.[227] The French act on corporate social responsibility, the Conflict Minerals Regulation and the unofficial German legislative proposal contain a due diligence-based complaints or alert mechanism for gathering information on operational risks.[228] Different types of company-internal complaints mechanisms are becoming more common. One example of this is the Whistleblowing Directive of the EU, under which companies with at least 50 employees must establish whistleblowing channels.[229] The directive will apply from December 2021. The whistleblowing channels may allow the company's employees, and optionally also stakeholders, to report on suspected or actual violations. Under the unofficial legislative proposal presented in Germany, the channel would also be available to a company's stakeholders. This is not explicitly mentioned in the French act but according to legal literature, this purpose is clear from the factual content.[230]

Requiring small companies to establish internal complaints channels may be problematic for the simple reason that in an enterprise with a small number of employees, keeping complaints anonymous is difficult. During the legislative process, introducing a complaints channel for medium-sized and large companies as part of the implementation of the Whistleblowing Directive could be considered.[231]

Consultations with company's stakeholders play an important role in the UN Guiding Principles, and should take place when identifying and assessing risks as well as when tracking the effectiveness of their response.[232] Under the French act on corporate social

226 Germany, Section 2 of NaWKG.

227 Principle 29 of the UN Guiding Principles.

228 France, Art. L. 225-102-4. – I; Article 4(e) of the Conflict Minerals Regulation; Germany, Section 9 of NaWKG.

229 Directive (EU) 2019/1937 of the European Parliament and of the Council of 23 October 2019 on the protection of persons who report breaches of Union law (Whistleblowing Directive).

230 Savorey 2020, p. 69.

231 The directive applies to certain breaches of Union law; see Article 2 of the Whistleblowing Directive.

232 See Principles 18 of the UN Guiding Principles. See also Principles 20 and 29.

responsibility, the company should engage its stakeholders in the preparation of its due diligence plan.[233] Engaging stakeholders in environmental decision-making is also a key principle in environmental law and stated in such documents as the Aarhus Convention. From the company's perspective, engaging the local community in environmental decision-making may be appropriate to gain the approval and trust of the local community (social licence).[234]

Environmental legislation includes provisions on the right to participate in decision making and access information. In addition, legislation on cooperation in companies also obliges companies to engage their personnel and stakeholders in their operations. Application of this legislation depends on the number of persons employed by a company.[235] It is not always necessary or essential to consult the stakeholders. Differences in consultation practices depending on the size of the company and the nature of its operations are also taken into account in the UN Guiding Principles.[236]

It is more difficult for companies to obtain information from their subcontractors or their subcontractors' subcontractors than from the companies and corporations under their control. Provisions in the existing reporting and due diligence legislation already require companies to describe their processes to verify their supply chains.[237] In practice, companies can introduce contractual terms requiring their subcontractors and suppliers to exercise human rights and environmental due diligence in their operations and to require this from their own subcontractors. However, supervising compliance with the contractual terms is difficult if not impossible, especially in long supply chains.[238]

The level of businesses' internal human rights and environmental expertise varies. The chance to use outside experts is one solution offered in UN Guiding Principles and legislation. For example, the Conflict Minerals Regulation requires that audits must be carried out via independent third parties.[239] Under the California **Transparency Act** (which is based on the reporting obligation), companies should state in their reports if their supply chains have not been audited by third parties.[240]

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233 France, Art. L. 225-102-4. – I; Savorey 2020, p. 69.

234 Kokko – Mähönen 2015, pp. 66–67.

235 See the Act on Co-operation within Undertakings (334/2007), which is applied to companies that regularly have at least 20 persons in employment relationship. The Act on Co-operation within Finnish and Community-wide Groups of Undertakings (335/2007) applies to groups of companies that have at least 500 employees in Finland and to Finnish companies within these groups of companies employing at least 20 persons.

236 Principle 18 of the UN Guiding Principles.

237 For example, France, Art. L. 225-102-4. – I; United Kingdom, Modern Slavery Act, 54(5)(c).

238 Study on Due Diligence, pp. 217–218.

239 Article 6 of the Conflict Minerals Regulation.

240 Transparency Act, Sec. 3(c)(1).

The auditing obligation laid down in the Conflict Minerals Regulation only applies to a limited range of areas and activities that are deemed as particularly risky. It would be more difficult to justify an auditing obligation covering a large number of sectors and linked to a widely applicable due diligence obligation. Moreover, there has also been criticism of external audits and certifications. The critics have, for example, highlighted the limited scope of the audits and the limited chances of the auditors to uncover possible abuses.[241]

5.2.3.2 Preventing adverse impacts and monitoring the effectiveness of the measures

After identifying adverse human rights and environmental impacts arising from their operations or risks of such impacts, companies should take measures to stop, prevent and mitigate such impacts. Offering remedies for impacts that have already arisen also plays an important role. However, as there are special issues concerning the regulation of the remedial measures, in this report they are discussed separately from the prevention of the impacts.

The content of appropriate preventive and mitigative measures varies, depending on whether the impact has already arisen or whether it is still a potential risk, and on whether the company has caused the impact or contributed to it or whether the effects are connected with the company's operations, for example on the basis of business relations.[242] Under the UN Guiding Principles, companies should also address impacts in situations in which impacts arise in their supply chains.[243] Preventing adverse impacts is based on their identification and this should take place in a proactive manner. Companies should also ensure that the impacts are being addressed by tracking the effectiveness of their response. The obligation of companies to prevent, mitigate or stop adverse impacts of their operations could also be laid down in the law.

Under the UN Guiding Principles, as part of the prevention of the impacts, companies should organise their operations so that the impacts can be effectively addressed.[244] Thus, the requirement is linked to the integration of due diligence into companies' operations. This can be carried out in a number of ways.[245] The OECD Guidelines give examples of practical measures when specifying environmental due diligence. The same measures can be used (and are already used) in human rights due diligence. As part of due diligence, companies should:

241 *Study on Due Diligence*, pp. 73–74; Lebaron – Lister 2015, pp. 905–924.

242 The Corporate Responsibility to Respect Human Rights – Interpretative Guide, 2012, p. 36–39.

243 Principle 19 of the UN Guiding Principles and Commentary to it.

244 Principle 19 of the UN Guiding Principles.

245 Principles 16 of the UN Guiding Principles.

1. establish a system of environmental management appropriate to the enterprise to collect information and set and monitor environmental targets;
2. provide the public and workers with adequate information on the environmental impacts of the activities of the enterprise and engage in a dialogue with stakeholders;
3. assess and address in decision-making environmental impacts associated with goods and services of the enterprise over their full life cycle; mitigate the adverse impacts if they cannot be prevented altogether;
4. implement cost-effective measures to prevent and avoid environmental damage in situations in which there is no full scientific certainty of the risks;
5. maintain contingency plans for preventing, mitigating, and controlling serious environmental and health damage, accidents and emergencies arising from their operations;
6. continually seek to improve corporate environmental performance, at the level of the enterprise and by adopting technologies and operating procedures in all parts of the enterprise; by developing and providing products or services that have no undue environmental impacts, are safe, reduce greenhouse gas emissions, are efficient in their consumption of natural resources, are recyclable or reusable; by providing consumers with information on the environmental impacts of their products and services; and by studying and assessing ways to enhance environmental efficiency by for example, developing strategies to reduce emissions and use resources more efficiently;
7. provide adequate education and training to workers in environmental and safety matters; and
8. contribute to the development of environmentally friendly and economically efficient social policy.[246]

Under the French act on corporate social responsibility, companies must make their due diligence plans public. The Dutch law requires that companies give an assurance on the use of child labour.[247] In Finland, too, companies must meet a range of different obligations concerning the preparation and publicity of policies.[248] A similar requirement could, in principle, also be included under the legislation on due diligence. However, preparation of policies and guidelines would place an administrative burden on companies and would not be suitable for small companies. From the perspective of protecting human rights and the environment, the weakness of written policies and

246 OECD Guidelines for Multinational Enterprises, VI. 1–8.

247 France, Art. L. 225-102-4. – I; The Netherlands, Article 4.

248 Under section 9 of the Occupational Safety and Health Act, the employer must have an occupational safety and health action plan in place; under Chapter 9, section 1, subsection 3 of the Anti-Money Laundering Act, operational guidelines on the procedures concerning customer identification must be in place; under Chapter 8, section 15 of the Act on Credit Institutions, credit institutions must keep details of their remuneration policies available on their websites.

guidelines is the difficulty of implementing them into practice in an efficient manner.[249] Making it mandatory to employ specific contractual terms in a company's contracts with their supply chains is hampered by the fact that companies can be in a very different negotiating position in relation to their subcontractors and suppliers. Also, SMEs usually have fewer resources to supervise compliance with such contractual obligations than large companies.[250]

Details of the training provided for the businesses' personnel may be included in the statements required under the legislation in California and the United Kingdom.[251] Under the unofficial legislative proposal presented in Germany, companies should designate a compliance officer supervising adherence to the legislation.[252] Similar provisions on company's internal supervision and training are also contained in other laws. For example, the Anti-Money Laundering Act contains provisions on training for the personnel and on designating a person monitoring compliance with the training obligation.[253] The General Data Protection Regulation contains provisions on the designation of a data protection officer who is responsible for supervising compliance with the regulation and for training the employees taking part in data processing.[254]

Companies may already have in place a range of different processes to identify and assess the impacts of their operations. For example, environmental management systems aim to help reduce adverse environmental impacts arising from companies' operations and to enhance positive impacts by systematically including environmental matters in operations and in operational planning.[255]

The Conflict Minerals Regulation lays down obligations concerning management systems and other concrete instructions for addressing operational issues. For example, the regulation contains provisions on structuring of internal management systems, control responsibilities, incorporation of supply chain policies, and a traceability system.[256] The Timber Regulation also contains a description of the information required for the due diligence system.[257] Such detailed requirements are possible because the regulations

249 *UN Working Group on the issue of human rights and transnational corporations and other business enterprises*, A/73/163, section 28.

250 Study on Due Diligence, p. 318.

251 United States, California, *Supply Chains*, Sec. 3(c)5; United Kingdom, Modern Slavery Act, 54(5)f.

252 Germany, section 8 of NaWKG.

253 Chapter 9, section 1 of the Act on Preventing Money Laundering and Terrorist Financing (444/2017, Anti-Money Laundering Act).

254 Articles 37 and 39(1)b of the Regulation (EU) 2016/679 of the European Parliament and of the Council on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC (General Data Protection Regulation).

255 Scherf et al. 2019, p. 56.

256 Article 4 of the Conflict Minerals Regulation.

257 Article 6 of the Timber Regulation.

only apply to one sector (and with respect to the Conflict Minerals Regulation, a certain geographical area) and they have been adopted to solve a concrete problem/risk: use of the revenue generated by the conflict minerals to feed violent conflicts in conflict regions and the problems created by illegal logging.[258] In such situations, the proportionality and reasonability of due diligence measures (deciding on the actions and the required information on the basis of the company's own assessment) play a less important role.

In theory, companies could be obliged to introduce specific systems or processes to assess the risks arising from their operations.[259] However, defining such systems and processes could be difficult, especially if the due diligence obligation would apply to a large number of companies and sectors. A proportionality assessment could also be included in the requirement concerning a company's systems and administration.[260] In principle, the legislation could also contain provisions specifying a company's obligation to exert its influence to prevent adverse impacts. It would also be possible to include provisions detailing situations in which preventive measures should be taken.[261] The obligation to monitor the effectiveness of measures taken could also be incorporated into legislation.

A separate question to consider is whether a company applying a specific standard or audit system, or a company issued with a specific certificate could, as a rule, be considered to exercise adequate due diligence in the manner described in the law.[262]

Companies incur costs from the actions required of them. Such costs include personnel costs, costs arising from the implementation and maintenance of systems and the use of outside experts. If it is decided to introduce legislation with a broad scope, the scope of the measures that can and should be required of companies should be considered because wide-ranging obligations imposed on all SMEs or all companies operating in low-risk sectors would not likely result in corresponding human rights or environmental benefits. If a decision is made to introduce obligations concerning whistleblowing channels, use of outside experts or training, the obligations could only apply to companies exceeding a specific size or companies operating in high-risk sectors.

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258 Recital 1 of the Conflict Minerals Regulation; recital 3 of the Timber Regulation.

259 For example, under section 30 c of the Medicines Act (395/1987), holders of marketing authorisations, marketing authorisations for the parallel import of medicinal products and registrations must have a pharmacovigilance system.

260 For example, under Chapter 7, section 1 of the Act on Credit Institutions, a credit institution's corporate governance must be comprehensive and proportionate with respect to the nature, scope and diversity of its operations.

261 See Germany, section 6 of, NaWKG; Switzerland, Art. 716abis CO (new) 2a.

262 For more information about the potential certification problems, see Study on Due Diligence, pp. 522–524 and the studies referred to in the publication.

Identifying and preventing adverse human rights and environmental impacts are the key elements of due diligence. A process involving both elements may include different measures depending on such matters as the size, sector and operating area of the company.

As a rule, companies are free to decide how they identify and prevent adverse impacts arising from their operations. Legislation could also oblige companies to take concrete measures such as introducing grievance mechanisms, incorporating contractual terms in their supplier contracts or consulting with their stakeholders at different stages of the process.

5.2.3.3 Reporting obligation

Under the UN Guiding Principles, companies should be prepared to communicate externally the impacts of their operations and how they address them.[263] Communication can take different forms and it can also be informal. Provisions on companies' annual reporting are already contained in a number of different laws: in addition to the obligation to prepare and register financial statements, companies also have a wide range of different disclosure obligations, which are based, for example, on being listed on a stock exchange or their operating sector.[264] The purpose of disclosure obligations is to make the companies' operations more transparent, allow stakeholders to assess the companies' operations and enhance trust in business operations.[265] For example, the reporting requirements laid down in the accounting legislation help to assess companies' business operations. At the same time, the purpose of NFI reporting is to enable the assessment of the companies' social responsibility.[266]

Reporting on companies' production may improve consumer protection by providing consumers with information to assess the companies' supply of products or services and their supply chains.[267] NFI reporting has also been suggested to enhance corporate governance.[268] However, based on available research data, there is only limited evidence that reporting has any direct positive impacts on companies' governance.[269] There are, however, some indications that reporting has increased the number of claims brought

263 Principles 21 and 29 of the UN Guiding Principles.

264 For example, provisions on the obligation to produce financial statements laid down in Chapter 3 of the Accounting Act; provisions on the reporting obligation of listed companies laid down in Chapters 6-10 a of the Securities Markets Act; provisions on the reporting obligation of extractive industry companies laid down in the Extractive Industries Act; provisions laid down in Chapter 8, section 15 of the Act on Credit Institutions on the obligation of credit institutions to keep details of their remuneration practices available on their websites.

265 OECD Guidelines for Multinational Enterprises, III.28, VI.65.

266 For example, SWD(2013) 127, p. 10.

267 For example, California, Sec. 2(i)–(j); Norway, sec. 1.

268 SWD(2013) 127, p.18 and the studies referred to in the document.

269 Study on Due Diligence, pp. 344–347.

against companies. Thus, a disclosure obligation may indirectly impact companies' operations through more effective stakeholder supervision.[270]

Under the French act on corporate social responsibility, companies must make their due diligence plans and details of their due diligence measures accessible to the public and publish them as part of their annual reports.[271] The obligation to make due diligence plans publicly accessible means that it is at least theoretically possible to assess the companies' due diligence measures in advance before any legal assessments arising from the adverse impacts. However, preparing reports and due diligence plans burdens companies with administrative costs. The general view is that the reporting required of companies is a particularly heavy burden on SMEs. The administrative burden on SMEs resulting from the reporting could be reduced by allowing such enterprises to submit free-form or short reports – or to exempt SMEs altogether from the reporting obligation. Poor quality and lack of comparability of the reports have been considered as the main problems arising from free-form reporting.[272] An obligation allowing the submission of free-form reports would generate little added value for stakeholders and other supervisory bodies. At the same time, however, because of the risk-based and context-specific nature of due diligence, it might be difficult to require companies to produce fixed-form due diligence plans or statements. This is particularly true of the due diligence obligation applying to all companies.

The disclosure obligation applying to Finnish companies could be implemented as part of the companies' annual reporting or by obliging the companies to publish reports on their operations on such channels as their websites. Already under existing legislation, limited liability companies, cooperatives, certain other corporations and other actors that are not SMEs and that are obliged to keep accounts must submit copies of their financial statements and annual reports for registration to the Finnish Patent and Registration Office.[273] The NFI statement must be submitted as part of the management report appended to the financial statements or as a separate document. The auditor of the company must check that the statement has been submitted.[274]

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270 For example, Koekkoek et al. 2017, 525; Study on Due Diligence, pp. 176–177. At the same time, companies have also indicated that the efforts to act in a responsible manner by for example, pledging to observe voluntary international responsibility standards may have led to legal proceedings against them on the basis of alleged failure to comply with the due diligence obligation; Study on Due Diligence, p. 228.

271 France, Art. L. 225-102-4. – I; Savorey 2020, p. 64.

272 For example, *Independent Review of the Modern Slavery Act* 2019, pp. 40–41; Study on Due Diligence, p. 247.

273 Chapter 3, section 9 of the Accounting Act.

274 Chapter 3 a, sections 1, 5 and 6 of the Accounting Act.

In Finland, adding the disclosure obligation to annual reporting obligation could be introduced by changing the Accounting Act or as part of a separate act.[275] In any separate act, companies could be obliged to submit the reports as part of the annual reporting required under the Accounting Act.[276] Depending on the content of the report and the scope of the obligation, provisions on the disclosure obligation could be added to the chapter of the Accounting Act containing provisions on the management report or it could be included in the NFI statement. If the obligation is supposed to cover a maximum number of companies and differ from the NFI reporting in terms of its content, it might be justified to oblige companies to submit the reports as part of the management report. Public-interest entities, public limited liability companies, cooperatives and private limited liability companies that are not micro-enterprises or small enterprises are obliged to produce a management report.[277] If it is decided to make the reporting obligation part of the obligation to produce the management report, a large number of enterprises obliged to keep accounts would fall outside the reporting obligation. As to the scope of the reporting obligation, it should be noted that investors and other stakeholders are primarily interested in large (listed) companies.[278] In fact, it could also be decided to limit the reporting obligation to companies exceeding a certain size and/or companies operating in high-risk sectors.

Especially the NFI reporting requirement contains requirements similar to those laid down in the existing legislation on corporate social responsibility.[279] In order to reconcile possible overlaps, the unofficial German legislative proposal would allow companies applying the NFI Directive to submit their reports in connection with the NFI statement.[280] A similar provision could also be used to avoid overlapping reporting obligations of the largest Finnish companies. Moreover, if the due diligence reporting or the reporting obligation would, on the basis of the scope of application, concern a large number of Finnish companies belonging to the same group, the administrative burden could be eased by allowing group companies to submit joint reports.[281]

275 There are also provisions on reporting obligations in corporate legislation, such as in Chapter 8 of the Limited Liability Companies Act. However, incorporating the changes into corporate legislation would require changes in a large number of acts.

276 Section 8 of the Extractive Industries Act.

277 Chapter 3, section 1, subsection 3 of the Accounting Act.

278 Recitals 3, 13 and 14 of the NFI Directive. Commentary to Principle 14 of the UN Guiding Principles.

279 See the United Kingdom, Modern Slavery Act; Australia, Modern Slavery Act.

280 Germany, Section 11 of NaWKG.

281 For example, under the *Modern Slavery Act* of the United Kingdom, each of the companies meeting the applicability requirements must, as a rule, produce its own statement. However, a group may decide to submit joint statements, which is often practicable in situations in which subsidiaries are part of the parent company's supply or purchasing chains; Home Secretary, *Transparency in Supply Chains. A Practical Guide,* pp. 23–24.

There could be at least two options for companies to meet their statutory reporting obligation: reports could be published as part of the company's annual reports, or companies could be obliged to submit separate reports and publish them on such outlets as their websites. In order to improve the quality and usability of the reports, it might be practicable to lay down legislative provisions and possibly also detailed guidelines on the content of the reports.

A disclosure obligation requiring companies to report on their human rights and environmental performance would allow their stakeholders and the authorities to assess the companies' operations.

The comparability of the reports with each other is important. As a disclosure obligation requires companies to allocate resources to producing the reports, the reporting obligation could be more limited in scope than the rest of the due diligence obligation. For example, it could be decided that only the largest companies are required to submit reports. Quality and comparability of the reports could be enhanced by providing guidelines clarifying the content of the reports.

5.2.4 Assessing operational due diligence

5.2.4.1 Regulatory options

Defining the content of the due diligence obligation is also relevant to the ex-post evaluation of due diligence. The question is important because a company should be able to invoke a due diligence defence – that is to avoid liability by showing that it had taken necessary precautions to prevent the harm – in situations in which a claim for damages has been brought against it. As a rule, two approaches to enacting due diligence legislation can be identified: (1) a general act containing a brief overview of the stages of the process [282] and emphasising the appropriateness and proportionality of due diligence; and (2) an act providing a tighter framework for due diligence and the activities coming under it.[283]

A general act is more flexible and adapts to different situations. This was an important consideration when the Finnish act on limited liability companies was revised in the early 2000s. In the memorandum on the revision of the limited liability companies act, the need for flexibility was argued for by stating that limited liability companies operate in every imaginable sector and have a wide range of financing structures. The memorandum continued by stating that it would seem clear against this background that company law should be flexibly applied, and companies should be allowed to produce solutions tailored

282 See for example, the French law; the Modern Slavery Act of the United Kingdom and the Modern Slavery Act of Australia.

283 See the Conflict Minerals Regulation.

to their own needs. At the same time, it would also seem that legislators are poorly placed to draft detailed regulation suitable for all companies.[284] In later reports, the solutions adopted as part of the Limited Liability Companies Act have generally been considered as successful.[285] It can be argued that for most the companies, there should be room for flexibility in the content of the due diligence obligation.

If a decision is made to enact legislation emphasising the **appropriateness** and **context-specific nature** of due diligence, the content of due diligence could be presented fairly briefly, for example, by describing the key elements of the obligation: 1) assessing the impacts of the enterprise's operations; 2) preventing and mitigating the identified adverse impacts; 3) monitoring the effectiveness of the measures; and 4) providing information about the measures. These measures can be specified by listing general factors that should be considered in due diligence, such as the risk-based and proportional nature and regular updating of the assessment, and consultation with stakeholders and/or vulnerable groups during different stages of the process. However, the legislation would not specify the information that companies should collect to assess risks, detail the risks that they should consider in specific situations, describe the measures that they should take to prevent risks or the indicators used to monitor the effectiveness of the measures.

The unofficial German legislative proposal specifies the appropriateness of the impact assessment by stating that the content of the assessment depends on the following factors: country-specific and sectoral risks, likelihood and seriousness of the potential impacts, and the size of the company and its chances of influencing the actor causing the impacts. According to the proposal, companies would also be required to prepare a more in-depth impact assessment in situations in which impacts have been identified.[286] A similar due diligence obligation based on a risk assessment is also laid down in the Anti-Money Laundering Act, under which the party subject to the reporting obligation must apply an enhanced procedure to identify the customer if the risk assessment indicates that the customer relationship or the business transaction involves a higher than normal risk of money laundering and terrorist financing.[287]

With legislation enacting reporting obligations, general provision on the content of reports have been criticised for 1) leading to ambiguities concerning the content of the obligation; and for 2) weakening the comparability of company reports.[288] Comparability of the due diligence measures does not, however, play the same role as the comparability

284 See Airaksinen – Jauhiainen 2000, p. 22.

285 OM 20/2016, p. 8.

286 Germany, Section 2 of NaWKG.

287 Chapter 3, section 10 of the Anti-Money Laundering Act.

288 *Independent Review of the Modern Slavery Act 2015: Final Report, pp. 41–42; Revision of the Non-Financial Reporting Directive*, Inception impact assessment - Ares(2020)580716.

of the reports aimed at providing stakeholders with information. Appropriateness means that there are differences between companies in the manner in which due diligence is implemented.

What remains to be addressed are concerns regarding the ambiguity of expectations on the companies. If a general act is enacted, it might be difficult for companies to assess what they should do to meet the due diligence requirement. A detailed description of the steps required for due diligence, by for example listing the factors that should be taken into account in the process, would make it easier for companies to understand what they are required to do. At the same time, this approach might lead to a situation in which due diligence is reduced to the review of a checklist. This risk of overregulation is also highlighted in a UN report, which recognises the need to achieve balance between the appropriateness of the due diligence and legal certainty of companies.[289]

Especially if a decision is made to adopt an act on corporate social responsibility applying to a maximum number of companies, wording leaving the due diligence process open might prove a workable alternative for an approach based on proportionality and risks. Legislation in which the exact content of the due diligence obligation is left open may, however, create uncertainty regarding the expectations placed on companies. This is particularly the case because many companies are still unfamiliar with human rights and environmental due diligence.[290] An open and flexible obligation would mean that courts will play a role in the interpretation of the legislation and formulation of case law. However, it would take many years for courts to formulate the case law. From the perspective of human rights and the environment, the danger is that an obligation that is perceived as ambiguous with regard to its content will not lead to corporate practices that are appropriate in terms of the protection of human rights and the environment.

The content of the obligation could be clarified by discussing methods of exercising due diligence in the law text, in the legislative history or in separate guidance. For example, the act could include an authorisation to issue more detailed guidelines on due diligence by decree or a provision authorising a public authority to issue more detailed guidelines on the content of due diligence.

289 *UN Working Group on the issue of human rights and transnational corporations and other business enterprises,* A/73/163, section 25; High Commissioner for Human Rights, *Improving accountability and access to remedy for victims of business-related human rights abuse: The relevance of human rights due diligence to determinations of corporate liability,* A/HRC/38/20/Add.2, section 17.

290 Study on Due Diligence, pp. 221–222.

The due diligence obligation could be formulated in general terms with the emphasis on *appropriateness*. Alternatively, the actions required for exercising due diligence could be defined as precisely as possible, with emphasis on legal certainty. When these alternatives are assessed, consideration should be given to such matters as the number of companies coming within the scope of the legislation.

5.2.4.2 Supplementary guidelines

In addition to including authorisations and/or references in the act itself or its preparatory material, human rights and environmental awareness and expertise in companies can also be enhanced in other ways. Non-binding guidance and advice can be provided by such parties as the authorities, trade associations, other business cooperation networks, non-governmental organisations and other interested parties. The guidelines can take into account companies of different sizes and operating in different business sectors.

As there is already a large amount of non-binding guidance, the content of due diligence could also be specified by referring to these documents. The UN Guiding Principles and the OECD Guidelines are the most important sources of due diligence guidance. However, the same principle of due diligence is also applied in other OECD guidelines and in a number of different sector-specific guidelines.[291] A variety of different solutions for making such references can be found in the existing and planned legislation: Companies are obliged to exercise due diligence in accordance with the OECD Guidelines or the UN Guiding Principles[292] or these documents are referred to as a possible framework for implementing the requirements.[293] One key aim of the national guidelines could, in fact, be to enhance the awareness and understanding among companies of the information contained in the existing guidelines.

Corporate due diligence practices can also be disseminated by developing corporate governance. For example, linking the remuneration of management of listed companies to corporate social responsibility criteria has been highlighted as one instrument promoting

291 For examples of guidelines that companies could be referred to, see; Study on Due Diligence, pp. 272–274.

292 Articles 4 and 5 of the Conflict Minerals Regulation. The Taxonomy Regulation is also intended to oblige companies applying it to assess compliance with its requirements through the due diligence process described in the UN Guiding Principles or the OECD Guidelines; EU Technical Expert Group on Sustainable Finance (TEG), *Taxonomy: Final report of the Technical Expert Group on Sustainable Finance*, March 2020, p. 32.

293 Recital 9 of the NFI Directive.

long-term strategy of corporate governance.[294] For example, in the United Kingdom, companies have been encouraged to take a more responsible approach by adding to the Companies Act a provisions on the management's obligation to consider environmental, human rights and social impacts in their decision-making.[295] In addition to using legislative means, corporate governance can also be improved by means of corporate governance codes[296] or other ownership-steering guidelines.[297] For example, the Finnish Government's resolution on ownership-steering in state-owned companies contains a section devoted to corporate social responsibility.[298] There is a great deal of discussion on governance development, and this topic is not discussed further in this report. However, it should be considered in the potential legislative process.

5.3 Other issues that should be considered in the law-drafting process

5.3.1 Definitions

5.3.1.1 Human rights

Definitions of the terms used in legislation also determine the content of the obligations laid down in the law. If companies are obliged to exercise human rights and environmental due diligence, it is important to define what is meant by the terms. Defining the terms makes legislation easier to understand and enhances legal certainty.

Human rights cover a broad range of different rights, which are laid down in a large number of international instruments.[299] In accordance with the UN Guiding Principles, human rights include **at least** the rights described in the Universal Declaration of Human

294 See the Directive (EU) 2017/828 of the European Parliament and of the Council amending Directive 2007/36/EC as regards the encouragement of long-term shareholder engagement. The remuneration provisions of the directive have been implemented in Finland by means of amendments to the Limited Liability Companies Act and the Securities Markets Act and by means of the Ministry of Finance decree on the share issuer's remuneration policy and remuneration report (608/2019).

295 United Kingdom, Companies Act 2006, Sec. 172. See Tsagas 2017. For more information about the extensive corporate law debate on the regulation of management due diligence, see for example, Lautjärvi 2017.

296 In Finland, listed companies must observe the Finnish Corporate Governance Code of the Securities Market Association (available: https://cgfinland.fi/wp-content/uploads/sites/39/2019/11/corporate-governance-code-2020.pdf). See also Mähönen 2019.

297 For proposals made from the perspective of sustainable development, see Sjåfjell et al. 2019.

298 Valtioneuvoston kanslia, *Vaurautta vastuullisella omistajuudella. Valtioneuvoston omistajapoliittinen periaatepäätös* 8.4.2020, Helsinki 2020.

299 UN Human Rights Council, *Protect, Respect and Remedy: A Framework for Business and Human Rights*, A/HRC/8/5 (7 April 2008), (section 6) states that companies can influence virtually all known human rights. Producing a list of human rights creates the risk that an essential right is left out.

Rights, the International Covenant on Civil and Political Rights, the International Covenant on Economic, Social and Cultural Rights, and the ILO Conventions.[300]

In the existing and proposed legislation, rights to be protected are defined, for example, by referring to international human rights treaties.[301] Finland has ratified the instruments referred to in the UN Guiding Principles and a number of other human rights treaties. In the possible legislation, human rights could be defined by making general references to internationally recognised human rights, the human rights treaties ratified by Finland, or the instruments referred to in the UN Guiding Principles and any other agreements considered important.[302] If human rights were to be defined by listing a number of human rights treaties, this could be done in an appendix to the act or in a decree issued separately. A similar approach is applied in the Act on Public Contracts, the appendix of which lists the international social, environmental and labour law conventions the breach of which the contracting entity can use as a discretionary exclusion criterion.[303]

Additional qualifiers can be used to set protection offered by the act at a certain level. For example, the French act on due diligence requires that serious violations of human rights must be prevented.[304] The concept of human rights or the concept of a serious violation of human rights are not specified in the act.[305] Under the UN Guiding Principles, severity of human rights impacts is judged by their scale, scope and irremediable character.[306] Irremediable character (or irreversibility) refers to the permanence of the impact. Thus, the seriousness of the violation would be defined on a case-by-case basis. If the severity of the human rights impacts would be used as a factor limiting the scope of the legislation, serious human rights impacts should also be defined.

Such crimes as human trafficking, inhumane treatment and systematic discrimination could be considered as serious human rights impacts.[307] However, this would substantially narrow the scope of the act and might lead to a situation, in which companies would not identify all human rights impacts central to their operations.[308] Instead of referring to

300 Principle 12 of the UN Guiding Principles.

301 Section 4 of the Australian Modern Slavery Act 2018 and article 2 of the Dutch act on child labour refer to the ILO Convention No. 182, which concerns the worst forms of child labour. A total of 16 different human rights treaties are appended to the unofficial German legislative proposal and the human rights referred to in the act are defined in the treaties.

302 Other agreements referred to in the legislation could consist of the agreements on vulnerable people; see https://www.ungpreporting.org/resources/how-businesses-impact-human-rights/.

303 Section 81(1)(5) of the Act on Public Contracts; Appendix C.

304 France, Art. L. 225-102-4. – II.

305 It has been proposed in the literature that the UN Guiding Principles and the OECD Guidelines should be used in the interpretation of the act; Savorey 2020, pp. 62–63, 65.

306 Commentary to Principle 14 of the UN Guiding Principles.

307 See the Norwegian legislative proposal, Sec. 5(2) and its justification; Mestad et al. 2019.

308 Of the debate on the definition of seriousness, see Zerk 2011, pp. 25–29; Pietropaoli 2020, pp. 25–26.

serious human rights impacts, companies could, in order to avoid potentially problematic definitions and ambiguities, be obliged to focus on the human rights impacts that are particularly relevant to their operations.[309] Even without detailed definitions, limiting the due diligence obligation to relevant impacts would narrow the scope of the obligation and encourage companies to focus on the identification and prevention of the risks that are particularly relevant to their operations.

5.3.1.2 The environment

Defining the environment is not an unambiguous task even though there are provisions on environmental regulation in a large number of Finnish acts.[310] However, it is difficult to find a precise definition of the environment in any of them.[311] In the Environmental Protection Act, the definition of environment can be derived from the definition of environmental pollution. Under the act, environmental pollution means such emissions that either alone or together with other emissions cause harm to health; are detrimental to nature and how it functions; prevent or materially hinder the use of natural resources; cause a loss of general amenity of the environment or of special cultural values; reduce the suitability of the environment for general recreational use; cause damage or harm to property or impairment of use; or constitute a comparable violation of the public or private interest.[312]

In the Act on Environmental Impact Assessment Procedure, the definition is approached by defining an environmental impact. Under the act, environmental impact means the direct and indirect effects of a project or operations on (among other things) soil, water, air, climate, flora, organisms and biological diversity; the urban structure, buildings, landscape, townscape and cultural heritage; and the utilization of natural resources.[313]

The Criminal Code refers to impairment of the environment in which somebody intentionally or through gross negligence, introduces, emits or disposes into the environment an object, a substance, radiation or something similar in violation of the law, a provision based on law, a general or a specific order, or without a permit required by law or in violation of permit conditions. Impairment of the environment can also occur by violating provisions of the acts and legislation mentioned in the Criminal Code.[314] The

309 Norja, Sec. 5(1).

310 Examples include the Act on Compensation for Environmental Damage (737/1994), Nature Conservation Act (1096/1996), Land Use and Building Act (132/1999), Act on Environmental Protection in Maritime Transport (1672/2009), Waste Act (646/2011), Emissions Trading Act (311/2011), Chemicals Act (599/2013), Environmental Protection Act (527/2014), and the Act on Environmental Impact Assessment Procedure (252/2017).

311 Ekroos et al. 2012, p. 3.

312 Section 5 of the Environmental Protection Act.

313 Section 2 of the Act on Environmental Impact Assessment Procedure (252/2017).

314 Chapter 48, section 1 of the Criminal Code.

international standard ISO 26000 defines environment as the natural environment in which an organisation functions, incorporating the air, water, land, natural resources, flora, fauna, people, outer space, and their mutual relationships.[315]

For this report, the key issue concerning the definition of the environment is whether the environment itself is deemed as an object of due diligence or whether environmental due diligence is relevant in situations, in which the protection of the environment also helps to protect human rights, such as the right to clean, safe, healthy and sustainable environment.[316] Internationally, the trend seems to be to treat the environment as an independent object of protection.[317] However, the formulation of case law is still in progress and it is not entirely clear whether due diligence is a suitable instrument for addressing all different types of environmental impacts. As regards the link between environmental and human rights impacts, it should be noted that even though environmental impacts do not always involve direct human rights impacts, indirect or long-term impacts are possible.[318] For example, preserving biodiversity, sustainable development and the action against climate change can also be seen as human rights measures: they help to ensure the right to enjoy environment and natural resources over generations.[319]

The purpose of the environmental legislation is not to prevent all adverse impacts of business operations on the environment. Operators may, if necessary, after an assessment procedure and/or an environmental permit process, carry out their activities within specific limits.[320] Private individuals are obliged to tolerate adverse impacts that are considered as normal. However, there is no obligation to tolerate personal injury, such as adverse health impacts.[321] If due diligence were to apply also to the environment itself, the framework within which environmental due diligence is assessed should be determined.[322]

315 ISO 26000:2010, 2.6.

316 For example, environmental damage can refer to damage caused through environmental disruption (such as pollution) or damage caused to the environment itself; Waris, Emil, "Ennallistaminen korjaamalla – ympäristövastuudirektiivin mukainen uuden sukupolven ennallistamisvastuu", Edilex 2009, pp. 18–19.

317 The NFI Directive, the French act on corporate social responsibility, the Swiss counter-proposal and the unofficial German legislative proposal also include obligations concerning the environment. See also Scherf et al. 2019, p. 15.

318 Study on Due Diligence, pp. 184–190; Special Rapporteur on extreme poverty and human rights, *Climate change and poverty*, A/HRC/41/39 (July 2019).

319 For example, COM(2020) 380.

320 See for example, section 52 of the Environmental Protection Act.

321 Hollo 2009, pp. 123–124.

322 Scherf et al. 2019, pp. 56–57.

Under the OECD Guidelines, companies should, within the framework of laws in the countries in which they operate, and *in consideration of relevant international agreements, principles and objectives*, take due account of the need to protect the environment, public health and safety, and generally to conduct their activities in a manner contributing to the wider goal of sustainable development.[323] Similar objectives are also laid out in such documents as the Environmental Protection Act.[324] Both in the Swiss counter-proposal and the unofficial German legislative proposal, the definition of the level of environmental protection refers to the international agreements binding on the countries.[325] Finland is a party to more than one hundred international environmental agreements, which include agreements focusing on specific themes, regional agreements and mutual agreements.[326] Definitions used elsewhere in environmental legislation could be used to formulate the legal interests to be protected and/or objectives to be incorporated into the act. References could also be made to key environmental agreements.[327]

Under the French due diligence legislation, environmental due diligence requires the prevention of serious personal injuries and adverse health and environmental impacts that might result from the company's operations.[328] The concept of seriousness is not specified in the legislation. The unofficial German legislative proposal would be applied to significant violations of fundamental requirements of environmental protection or environmental degradation.[329] There are references to significant environmental impacts elsewhere in the Finnish environmental legislation.[330] The significance criteria of environmental impacts is met when the project is of specific type or size or on the basis of case-by-case assessment.[331] Adding specifications detailing the character of the environmental impacts referred to in the law influences the scope of due diligence. Because environmental impacts differ in nature from human rights impacts, determining whether to set a specific harm threshold should be carried out separately from the human rights assessment. If such matters as significant environmental impact is not defined in the law, interpreting significance could be on the basis of other environmental legislation.

323 OECD Guidelines for Multinational Enterprises, VI.

324 Section 1 of the Environmental Protection Act.

325 Sections 2, 3 and 8 of NaWKG; 716abis section 6 of the Swiss counter-proposal.

326 Ympäristöministeriö, *Kansainväliset ympäristösopimukset ja Suomi*.

327 For example, Ympäristöministeriön 'Keskeiset kansainväliset ympäristösopimukset sekä niiden tavoitteet ja toteutuminen', (available: https://www.ym.fi/download/noname/%7BDDC31061-F914-4DF6-9483-E2C2F57B5E10%7D/146070).

328 France, Article L. 225-102-4. – I.

329 Germany, section 3(10) of NaWKG.

330 For example, the environmental impact assessment procedure is well-suited for projects and project changes that are likely to have *significant* environmental impacts; section 3 of the Act on Environmental Impact Assessment Procedure.

331 Section 27 of the Environmental Protection Act, section 3 of the Act on Environmental Impact Assessment Procedure and Appendix 2, which presents factors that should be considered in the case-by-case assessment.

Human rights are defined in international agreements.

The environment can be defined in many different ways. Environmental impacts can be roughly divided into two parts: 1) impacts producing human rights effects; and 2) impacts that only affect the environment. In the preparation of a corporate social responsibility act, it should be decided which is the object of legal protection in environmental due diligence.

From the perspective of applying and interpreting the act, qualifiers, such as **serious**, **significant** or **essential**, which narrow the scope of the act, may be added to the definition of human rights and environmental impacts. The appropriateness of these additional qualifiers should be assessed separately for human rights and the environment.

5.3.1.3 Supply chains and value chains

Under the UN Guiding Principles, companies can also generate adverse impacts indirectly through their business relationships.[332] Businesses can decentralise their production processes through subsidiaries and long outsourcing and subcontracting chains, geographically and organisationally. Businesses' production chains can cover both actors in direct contractual relationships with the businesses and contractual partners of these actors, with no direct contractual relationships with the businesses. The structures can be defined as supply chains or value chains.[333]

The term 'value chain' is used in the UN Guiding Principles. The term 'supply chain' is used in corporate social responsibility legislation though its meaning may vary.[334] The term 'supply chain' is also used in the national legislation.[335] When the supply chain is defined, it is essential to define, how far in the company's supply chain the due diligence requirement extends.

332 Principle 13 of the UN Guiding Principles.

333 Salminen – Rajavuori 2019, p. 388.

334 Salminen – Rajavuori 2019, p. 401.

335 For example, Medicines Act (395/1987); Act on the Safety of Toys (1154/2011).

5.3.1.4 Enterprise

Due diligence obligation applies to enterprises.[336] An enterprise is not defined in the UN Guiding Principles. Under the OECD Guidelines, the concept refers to an enterprise engaged in economic activities or other entity that is capable of coordinating the activities of its units in different ways.[337] In Finland, business activities can take place under a broad range of different legal forms. Limited liability company is the most common business form in Finland. The number of general partnerships, limited partnerships and cooperatives is smaller.[338] However, there are also cooperatives and limited partnerships posting substantial sales and balance sheets. Foundations and associations can also be engaged in business activities. There are a number of different acts in Finland containing provisions on specific business forms.[339] In the Finnish public sector, central government and municipalities are engaged in business activities through their ownership of companies operating in the market. These companies fall within the scope of application through other legislation. Municipalities and central government may also own unincorporated enterprises to which separate legislation applies.[340] Limiting the scope of the act to a specific company form would be difficult to justify.

Finnish subsidiaries of foreign groups of companies account for a large proportion of business operations in Finland in many sectors.[341] Foreign companies can also engage in business operations in Finland by establishing branches. Services can also be offered in Finland without establishing a branch or other registered corporations in our country. In that case, the service provider does not come within the scope of the Finnish corporate legislation or the Finnish Accounting Act. However, such companies can register as taxpayers in Finland.[342]

Instead of listing different legal forms falling under the scope, legislation may contain general references to businesses or undertakings (or the business activities carried

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336 The UK act applies to registered corporations and partnerships; Home Secretary, T*ransparency in Supply Chains. A Practical Guide*, p. 8. The Australian act also applies to trusts, publicly owned companies, and companies liable to pay taxes in Australia; Section 4, 5(1) of the Modern Slavery Act 2018. There has been debate in France on whether Sociétés par Actions Simplifiées (S.A.S) companies come within the scope of the French due diligence legislation; Brabant – Savorey 2017a, pp. 3–5.

337 OECD Guidelines, p. 17.

338 Number of businesses in the Finnish Trade Register. Private traders (self-employed persons) are also included in the statistics of the Finnish Patent and Registration Office. However, as a private trader has the same status as a legal person and enterprise as other businesses, private traders are not discussed in this report.

339 Limited Liability Companies Act, Cooperatives Act, Partnerships Act (389/1988), Foundations Act and Associations Act. There is also special legislation containing provisions on companies operating in specific sectors, such as insurance companies and credit institutions.

340 Chapter 9 of the Local Government Act (410/2015); Act on Unincorporated State Enterprises (1062/2010).

341 Official Statistics of Finland (OSF): Foreign affiliates in Finland [e-publication]. ISSN=2242-2552. 2018, Appendix figure 2. Foreign affiliates share of overall entrepreneurial activity in Finland by industry in 2018. Helsinki: Statistics Finland [referred to on 4 May 2020]. Access method: http://www.stat.fi/til/ulkoy/2018/ulkoy_2018_2019-12-19_kuv_002_en.html.

342 See section 3 of the Business Information Act (244/2001).

out).[343] The definition of business activity is extensive and it covers activities that can be left outside the scope of corporate social responsibility legislation (such as the business activities of natural persons and estates).[344] The above-mentioned entities could be left outside the scope of the legislation by only applying the act to legal persons under private law registered in the Business Information System.[345]

5.3.2 Scope of application

5.3.2.1 Applying the act to companies of different sizes

The obligations of companies vary, depending on their size, sector and area of operations. Under the UN Guiding Principles, all companies must exercise due diligence, irrespective of their size and other factors. In its Study on Due Diligence (2020), the European Commission considered the following regulatory options: 1) due diligence obligation applying to large companies; 2) due diligence obligation applying to all companies; and 3) due diligence obligation applying to all companies, in addition to which the largest companies would also be subject to obligations concerning such matters as environmental targets.[346]

In the existing legislation, the due diligence obligation is applied by narrowing the content of the obligation (for example, by applying the obligation only to specific types of serious human rights violation, such as human trafficking), or by reducing the number of companies falling within the scope of the legislation. France, the country with the most extensive human rights and environmental due diligence obligation, has decided to significantly narrow the scope of the obligation. It applies to French companies that have at least 5,000 employees in France or 10,000 employees in France and in other countries.[347] If similar criterion were to be applied in Finland, the Finnish act would apply to about 30 Finnish companies. The Dutch act on the use of child labour applies to all companies selling products or services to Dutch end-users, irrespective of their size but its due diligence obligation is significantly less extensive that the obligation contained in the French act.

The legislative proposals presented in Germany and Switzerland would impose a due diligence obligation on both human rights and the environment. In both proposals, the scope of the obligation is broader than in the French act: under the Swiss proposal,

343 Section 1 of the Trade Register Act (129/1979) refers to private traders, while section 1 of the Restructuring of Enterprises Act (47/1993) refers to business operations.

344 See section 2 of the Business Information Act (244/2001).

345 In section 3(1)(3) of the Business Information Act, the following entities are considered as legal persons under public law: central government and central government agencies, municipalities, joint municipal authorities, parishes and other religious communities, and other legal persons under public law.

346 Study on Due Diligence, pp. 254–256.

347 France, Article L. 225-102-4.-I.

the thresholds for balance sheet and net sales are significantly higher than in the NFI Directive,[348] while in the unofficial German legislative proposal,[349] the limits are the same as those set for large undertakings in the Accounting Directive.[350] As a new element, exemptions based on risk assessments would be possible under both proposals.

In the existing and proposed legislation, the key restriction concerning the scope of application usually pertains to the size of the enterprise, which is determined on the basis of the balance sheet total, net sales and personnel, all indicators used in the accounting legislation.

The question of how to determine the size of the companies coming within the scope of the legislation would also be a key issue in any Finnish act on corporate social responsibility. Limiting the scope of the legislation on the basis of the company size would directly impact the number of enterprises to which the act would apply. At the moment, there are about one hundred large public-interest undertakings in Finland coming within the scope of NFI reporting. If the number of employees is used as the sole criterion, in 2018, of a total of 286,042 Finnish enterprises (excluding agriculture, forestry and fisheries), 657 were large enterprises (at least 250 employees), 2,995 were medium-sized enterprises (between 50 and 249 employees), 16,498 were small enterprises (between 10 and 49 employees), and 265,894 were micro-enterprises (between 1 and 9 employees).[351] Placing large enterprises, large and medium-sized companies, large companies and SMEs or all companies within the limits of the due diligence obligation significantly impacts the number of enterprises within the scope of the obligation.

The table below shows examples of the thresholds laid down in the law that could also be used as models for thresholds in the act on corporate social responsibility.

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348 The NFI reporting obligation applies to large public-interest undertakings that have exceeded at least two of the following thresholds on the balance sheet date both in the last completed financial year and in the financial year immediately preceding it: 1) balance sheet total EUR 20 million; 2) net sales or corresponding revenue EUR 40 million; 3) an average of 500 employees during the financial year.

349 This is a leaked legislative proposal and it is not based on an official legislative initiative.

350 A large undertaking is an enterprise exceeding at least two of the following three thresholds on the balance sheet date of the last completed financial year and the one immediately preceding it: 1) balance sheet total EUR 20 million; 2) net sales or corresponding revenue EUR 40 million; 3) an average of 250 employees during the financial year.

351 See the entrepreneurship statistics of the Federation of Finnish Enterprises (https://www.yrittajat.fi/sites/default/files/entrepreneurship_statistics_2020.pdf). The figures are based on the enterprise data of Statistics Finland. Agriculture, forestry and fisheries are not included in the statistics; see https://www.tilastokeskus.fi/tup/suoluk/suoluk_yritykset_en.html#Enterprises%201),%202018. The ratios for micro-enterprises and small enterprises in the 2013 statistics based on the thresholds laid down for the same categories in the Accounting Act are very similar; HE 89/2015 vp, pp.19–20.

	Legislation	Definition/companies to which the obligation would apply
Micro-undertaking	Chapter 1, section 4 b of the Accounting Act; Article 3(1) of the Financial Statements Directive.	An entity exceeding **only one** of the following thresholds on the balance sheet date of the last completed financial year and the one immediately preceding it: 1) balance sheet total EUR 350,000; 2) net sales EUR 700,000; or 3) an average of 10 employees during the financial year.
Small undertaking	Chapter 1, section 4 a of the Accounting Act; Article 3(2) of the Financial Statements Directive.	An entity exceeding **only one** of the following thresholds on the balance sheet date of the last completed financial year and the one immediately preceding it: 1) balance sheet total EUR 6,000,000 (under the Financial Statements Directive, the limit is EUR 4,000,000); 2) net sales EUR 12,000,000 (under the Financial Statements Directive, the limit is EUR 8,000,000); or 3) an average of 50 employees during the financial year.
Medium-sized undertaking	Article 3(3) of the Financial Statements Directive. This definition is not contained in the Accounting Act.	An entity that is not a micro-undertaking or a small undertaking and that exceeds **only one** of the following thresholds on the balance sheet date: 1) balance sheet total EUR 20,000,000; 2) net sales EUR 40,000,000; or 3) an average of 250 employees during the financial year.
Large undertaking	Chapter 1, section 4 c of the Accounting Act; Article 3(4) of the Financial Statements Directive.	An entity exceeding **at least two** of the following thresholds on the balance sheet date of the last completed financial year and the one immediately preceding it: 1) balance sheet total EUR 20,000,000; 2) net sales EUR 40,000,000; or 3) an average of 250 employees during the financial year.
Public-interest entity	Chapter 1, section 9 of the Accounting Act.	A Finnish entity that has issued a share, bond or another security subject to trading on a regulated market referred to in Chapter 2, section 5 of the Securities Markets Act (746/2012); A credit institution referred to in Chapter 1, section 7 of the Act on Credit Institutions (610/2014) and an insurance company referred to in Chapter 1, section 1 of the Insurance Companies Act (521/2008).
Non-financial reporting obligation	Chapter 3 a, section 1 of the Accounting Act; NFI Directive.	**Large** public-interest undertakings that have an average of **more than 500 employees** during the financial year.
Obligation to appoint an auditor	Chapter 2, section 2 of the Auditing Act	There is no obligation to appoint an auditor for a corporation in which **only one** of the following conditions was met in the last completed financial year and the one immediately preceding it: 1) balance sheet total exceeds EUR 100,000; 2) net sales or comparable revenue exceeds EUR 200,000; or 3) the average number of employees is more than three.
Obligation to appoint a KHT auditor or a KHT audit firm	Chapter 2, section 5 of the Auditing Act	A corporation traded in the regulated market or if the corporation/foundation meets **at least two** of the following requirements in the last completed financial year: 1) balance sheet total exceeds EUR 25,000,000; 2) net sales or comparable revenue exceeds EUR 50,000,000; or 3) the corporation/foundation has an average of more than 300 employees.

Narrowing the scope of application on the basis of the company size has been considered particularly important in order to ease the administrative burden of small enterprises.[352] In enacted national due diligence legislation and legislative proposals, an extensive due diligence obligation, covering human rights and the environment, is typically connected with the narrowing of the scope of application to companies exceeding a specific size. This is partially based on the view that an obligation that would treat all companies in the same manner would, in relative terms, be a heavier financial burden on SMEs than on large companies.[353] At the same time, it should also be noted that the due diligence laid out in the UN Guiding Principles takes into account different company sizes and the risks associated with their operations. The due diligence required of micro-enterprises or SMEs operating in low-risk sectors would therefore differ from the due diligence exercised by large multinational listed companies, both in terms of content and costs.[354] Some of the obligations that might be attached to due diligence are such that adjusting their content to the needs of small companies would not necessarily be practicable. In such cases, obligation-specific application limits could be considered. For example, only obliging companies of specific size to submit reports could be considered to limit incurred administrative costs.

5.3.2.2 Narrowing the scope on the basis of the business sector or geographical region

The scope of the legislation could also be narrowed by introducing legislation that only applies to certain high-risk sectors. For example, the Conflict Minerals Regulation of the EU only applies to specific operations (imports of conflict minerals). Furthermore, the provisions of the regulation only apply to conflict regions. Narrowing the scope of the legislation to operations in specific areas has been criticised for prompting companies to move their operations to areas where the legislation does not apply.[355] Legislation that would only apply to conflict regions in general could also be an option. UN guidelines could be used as interpretative guide in the definition of conflict regions.[356] If it is decided not to list conflict regions, there would be room for interpretation in the act concerning its scope. Instead of using regional definitions, the scope of the act or specific obligations contained in it could also be determined on the basis of an undertaking's sector.

Transboundary operations of large businesses are often in substantial scale. However, SMEs may also have major impacts on human rights and the environment, depending on

352 See COM(2011) 803; TEM 27/2018, pp. 99–102.

353 For example, Study on Due Diligence, p. 318.

354 Principle 14 of the UN Guiding Principles.

355 According to a report, the obligation laid down in the Dodd-Frank Act under which the raw materials used by companies should not be connected with the conflict in Congo has prompted companies to move their operations elsewhere; Study on Due Diligence, pp. 350–351, 354 and the sources referred to in the report.

356 UN Global Compact – PRI 2010, p. 7.

their sectors and operating locations. In legislative terms, the matter could be solved by narrowing the scope of the act to large enterprises and by adopting an exemption under which the act can also apply to companies operating in high-risk sectors irrespective of their size or to SMEs exceeding certain size. For example, under the Swiss counter-proposal, the due diligence obligation would apply to companies that do not exceed the threshold but are engaged in operations involving a particularly high human rights and environmental risk. At the same time, however, the provision would not apply to particularly low-risk companies exceeding the threshold. The unofficial German legislative proposal would also apply to medium-sized companies operating themselves or through enterprises under their control in high-risk sectors or conflict regions.[357] Small enterprises would be outside the scope of the act regardless of their sector.[358]

Particularly high-risk operations are not defined in the Swiss legislative proposal, but the unofficial German proposal includes a list of sectors considered high-risk: 1) agriculture, forestry and fisheries; 2) mining and quarrying; 3) manufacture of food products; 4) manufacture of textiles; 5) manufacture of clothing; 6) manufacture of leather goods and footwear; 7) manufacture of computers and electronic and optical products; and 8) electric, gas, heating and air conditioning.[359] The OECD has also prepared due diligence guidelines for some of these sectors.[360]

If Finland would decide to narrow the scope of due diligence (or some of its elements) on the basis of the risks associated with business operations, high-risk operations should also be defined in Finland. High-risk operations could be defined in an act or in a decree. If it is decided not to define high-risk operations by law or in a decree or guidelines issued under the law, the task would be left to the companies themselves and, if necessary, to the courts. Failing to define high-risk operations would thus create uncertainty regarding the scope of the act.

If the high-risk nature of business operations is used to extend the scope of act, it should also be considered when the link between a business and high-risk operations is sufficient. Under the unofficial German legislative proposal, a company's risk-based due diligence obligation would apply to the operations of the company itself or the operations of the

357 Switzerland, Art. 716abis CO; Germany, Section 2 of NaWKG.

358 A medium-sized enterprise is an enterprise exceeding only one of the following thresholds: 1) balance sheet total EUR 20 million; b) net sales EUR 40 million; c) an average of 250 employees during the financial year. Under the proposed German act, a small enterprise is an enterprise exceeding only one of the following thresholds: a) balance sheet total EUR 6 million; b) net sales EUR 12 million; c) an average of 50 employees.

359 Germany, section 3(6) of NaWKG. The sectoral classification in the section refers to the Regulation (EC) No 1893/2006 of the European Parliament and of the Council establishing the statistical classification of economic activities NACE Revision 2 and amending Council Regulation (EEC) No 3037/90 as well as certain EC Regulations on specific statistical domains.

360 See OECD Due Diligence Guidance for Responsible Business Conduct.

enterprises under its control. The company would not be subject to the due diligence obligation through its subcontractors. In theory, a limitation of this type might prompt entities to organise their high-risk activities through subcontractors. At the same time, however, if the operations of any part of an entity's supply chain could lead to the application of the legislation, companies might have to conduct extensive assessments, merely to solve whether the act applies to them.

The existing due diligence legislation only apply to entities of certain size and this is also the case with the proposed laws. Similar limitations should also be considered in Finland. Introducing a limitation that would only apply to certain parts of the obligation (such as reporting) is also to be considered.

Alternatively, the scope of application could be narrowed on the basis of the entity's sector or area of operations. A risk-based scope of application could be connected with other limitations, by for example, imposing a due diligence obligation on large enterprises and (small and medium-sized) enterprises operating in particularly high-risk sectors. When applying limitations concerning risk-based operations, high-risk operations should also be defined in the law.

5.3.2.3 International dimension of due diligence

Under the UN Guiding Principles, companies should respect human rights irrespective of where they operate.[361] Under the guidelines, in situations in which national legislation is in conflict with internationally recognised human rights or environmental requirements, enterprises should observe the national legislation, while at the same time endeavouring to respect human rights and the environment.[362] Regulating the operations of multinational enterprises by legislative means is limited by the principle of sovereignty, which is laid down in international law and under which a country may not exercise public authority in the territory of another country.[363]

The existing national laws only apply within national boundaries and this would also be case with proposed legislation: The legislation in California and the United Kingdom as well as the unofficial German legislative proposal apply to enterprises operating in these territories. The Dutch act applies to sales taking place in the Dutch territory. The French act on corporate social responsibility and the Swiss (counter-)proposal apply to companies registered in France and Switzerland. The Australian act applies to entities that are registered in Australia, controlled from Australia or that must pay taxes to Australia.

361 Commentary to Principle 11 of the UN Guiding Principles.

362 Principle 23 of the UN Guiding Principles; OECD Guidelines, I.2.

363 Section 1 of the Constitution of Finland; Saraviita 2011, p. 45. Sovereignty of the state is not unlimited. Finland may undertake to limit its sovereignty to safeguard human rights.

Likewise, the Conflict Minerals Regulation of the EU regulates conflict minerals imported to the European Union and the Timber Regulation timber imports to the EU.

Finnish legislation is binding on entities operating in Finland and entities registered in Finland.[364] When operating abroad, businesses primarily comply with local legislation.[365] However, the legislation applicable to a business partly depends on whether the operations are carried out by a group or whether they are outsourced to a local actor.

Companies, in which a Finnish company exercises control under the provisions of the Accounting Act, are considered subsidiaries.[366] A subsidiary is a legal person operating separately from its parent company and it is responsible for meeting its own obligations.[367] A subsidiary operating in another country complies with local legislation. A parent company can, on the basis of its control, supervise and steer the operations of its subsidiaries. A company can, for example, decide that its group applies standards that exceed the requirements laid down in local legislation in at least some of the areas in which the group operates. However, companies are not obliged to do this.[368]

By regulating the operations of a (parent) company located in one country, the impact of the legislation can also be extended outside the borders of national states. For example, a company producing consolidated financial statements in accordance with the Accounting Act must also prepare the annual report required under the Extractive Industries Act on its group companies.[369] Companies subject to the due diligence obligation laid down in the French act on corporate social responsibility must prepare a due diligence plan that also applies to enterprises under the company's control as well as suppliers and

364 For example, the Limited Liability Companies Act (Chapter 1, section 1) applies to all limited liability companies registered under the Finnish law, unless otherwise provided in the law.

365 A permanent establishment is considered to be part of the Finnish corporation and the requirements and obligations imposed on it may therefore also apply to a Finnish corporation. The permanent establishment must also comply with the local legislation applicable to its operations.

366 Under Chapter 1, section 5 of the Accounting Act, a company exercises control over another company if:

- the company has more than half of the voting rights based on the shares of the object company;
- the company has the right to appoint or dismiss the majority of the members of the object company's board or similar body; or
- the company has actual control over the object company in any other way.

367 DGEP 2019, p. 15.

368 For example, Zerk 2011, pp. 45–46. However, in Vedanta v. Lungowe Symposium, the United Kingdom Supreme Court concluded that the parent company (Vedanta) based in the United Kingdom had incurred a duty of care in relation to the operations of its Zambian-based subsidiary on the basis of public statements and the statements issued on the company's operations and its internal practices; http://opiniojuris.org/2019/04/18/symposium-duty-of-care-of-parent-companies/; Study on due Diligence, pp. 227–228.

369 Section 4 of the Extractive Industries Act. The obligation is not applied if a Finnish parent company is a subsidiary of a parent company based in the European Economic Area and when the parent company is prevented from exercising its control over the subsidiary on a prolonged basis.

subcontractors, at least on the first tier.[370] The company's obligation to also include its subsidiaries and business partners in the plan, extends the impact of the legislation beyond the French borders.

A company may organise its operations in foreign countries by means of outsourcing and subcontracting chains. The subcontracting chains may be long. These supply chains may consist of suppliers or subcontractors that are in direct contractual relationship with the company (first tier) and of their own suppliers and subcontractors with which the company does not have a direct contractual relationship (second tier). Subcontractors are legal persons independent of the company. In this case, the company itself does not incur an obligation to comply with local laws. The responsibility rests with local subcontractors. Moreover, a company can rarely be held legally liable for the operations of its subcontractors or their subcontractors.[371]

Under the UN Guiding Principles, corporate due diligence covers all operations of a business enterprise and the operations to which the enterprise is linked through its business relationships.[372] There are different legislative approaches to extending due diligence to a company's supply chains.[373] The French act extends the due diligence obligation to at least the first-tier subcontractors.[374] The due diligence obligation laid down in the Conflict Minerals Regulation of the EU covers the entire supply chain.[375] Under the Swiss counter-proposal and the unofficial German legislative proposal, the due diligence obligation would also apply to a company's operations in foreign countries. Under the Swiss counter-proposal, the due diligence obligation would apply to the impacts arising from the company's business relations. Under the German proposal, impacts of the company's operations arising from third parties would also be within the scope of the due diligence obligation.[376]

If the due diligence obligation were to apply throughout the supply chain, the content of the due diligence would be determined on a case-by-case basis. It may be unreasonably difficult for an enterprise to exercise due diligence throughout its supply chains and this is also taken into account in the UN Guiding Principles. In such situations, a business enterprise could focus its attention on areas, operations or subcontractors involving the

370 Code du commerce, article L. 225-102-4. -I, par. 4. Under the French act, the due diligence obligation applies to subcontractors and suppliers with which the company has an established commercial relationship. In legal literature, the definition has been considered ambiguous; Savorey 2020, p. 67.

371 Salminen – Rajavuori 2019, pp. 392–393.

372 Principle 17 of the UN Guiding Principles.

373 See Salminen – Rajavuori 2019, pp. 401–405.

374 Salminen – Rajavuori 2019, p. 403.

375 Article 4 of the Conflict Minerals Regulation.

376 Switzerland, Art. 716abis of the Code of Obligations; Germany, sections 2 and 5 of NaWKG.

highest risks.[377] For example, the Dutch act covers the entire supply chain but explicitly states the assessment is based on material that can be reasonably assumed to be known and available to the company.[378]

With regard to the international dimension of the legislation, attention should also be drawn to the distinction between the due diligence obligation concerning the enterprises controlled by the company or its supply chain, and the liability imposed on the company for damages. The scope of application could be set differently for different obligations. Even if the due diligence obligation were to be extended to the enterprises' supply chains, any liability for damage could only apply to the operations of the subsidiaries controlled by the enterprise.[379]

Finnish legislation applies to companies registered in Finland and companies operating in Finland. By obliging Finnish companies to exercise due diligence in their supply chains, the impact of the legislation could be extended beyond Finland's borders.

One of the legislative issues to be considered is how far a company should exercise such due diligence in its supply chain. Due diligence could apply to the entire supply chain or be limited to the corporations controlled by the company and its business partners. Extensive due diligence would be limited by its appropriateness. Moreover, the liability of the company to compensate for the adverse environmental and human rights impacts arising from its operations could be more limited than its obligation to exercise due diligence.

5.3.3 Supervision and sanctions

5.3.3.1 Supervision of due diligence

Enforcement of statutory obligations is enhanced by supervision and sanctions. With regard to environmental and human rights due diligence, the aim may also be to implement remedial action. Supervision may be directed at a company both before the adverse environmental or human rights impacts have arisen (ex-ante control) and after that (ex-post control). In environmental law, ex-ante control is performed, for example, by means of permits issued by the authorities or prior notification requirements. For example, projects that cause a risk of environmental pollution defined in the Environmental Protection Act require an environmental permit, notification or registration.[380]
Projects that are likely to have significant environmental impacts also require an ex-ante

377 Commentary to Principle 17 of the UN Guiding Principles.

378 The Netherlands, Article 5(2).

379 The Swiss due diligence obligation applies to a company's business operations but the liability for damage is limited, Switzerland, Art. 716abis CO; Art. 55 CO.

380 Chapters 4 and 5 of the Environmental Protection Act.

environmental impact assessment.[381] In addition to such project-specific impact assessments, companies must also be continuously aware of the impacts of their operations (duty to know).[382]

In addition to project-specific ex-ante supervision, companies' operations can also be supervised by means of reporting requirements and audits. The reporting requirements of existing corporate social responsibility laws are based primarily on supervision by stakeholders, which can be complemented by legal enforcement. For example, a court or the authorities may oblige a company to publish reports on pain of a conditional fine.

In California and in the United Kingdom, the failure to observe the disclosure obligation can lead to a court order to publish the report. In the United Kingdom, continuous negligence may also lead to fines.[383] The Australian act contains provisions on centralised supervision. Instead of being published on the companies' own websites or as part of their annual reporting, the statements are entered into a centralised register, which is publicly accessible. If the company fails to submit the statement and does not correct its action upon request, the name of the company and its failure to comply with the requirement may be published.[384] Under the French act on corporate social responsibility, a court may order a company to prepare and publish its due diligence plan and the report on its implementation on pain of a fine. The court may also decide to make its decision public.[385] Centralised supervision and the option of publishing details of companies that fail to comply with the law may make it easier for the markets to supervise compliance. Failure to observe the reporting obligation could, in principle, also be used as a ground for exclusion in public contracts.[386] Any ex-ante control could thus be made part of the companies' reporting obligation.

The statutory supervisory duties would be the responsibility of the authorities. Under the Timber Act, the Finnish Food Authority (previously the Agency for Rural Affairs) is responsible for supervising the implementation of the Timber Regulation and for acting as a supervisor.[387] Supervision required under the Conflict Minerals Regulation is the responsibility of the Finnish Safety and Chemicals Agency (Tukes). The Timber Regulation and the Conflict Minerals Regulation apply to specific sectors and the placing of specific products on the market. The protection of human rights and environmental due diligence is a wide area and would cover a broad range of very different actors. Finding a suitable

381 Act on Environmental Impact Assessment Procedure (252/2017).

382 Section 6 of the Environmental Protection Act. See also Kokko – Mähönen 2015, pp. 37–38.

383 California, Sec. 3(d); United Kingdom, Modern Slavery Act, Sec. 54(11).

384 Australia, Modern Slavery Act 2018, 16A.

385 France, Art. L. 225-102-4. – II.

386 Of the discretionary exclusion criteria in public contracts; see section 81 the Act on Public Contracts.

387 Section 4 of the Timber Act.

supervisory authority may prove difficult. If it is decided to leave the supervisory duty to the authorities, it should be decided, which authority or authorities would be made responsible for the task.

Official supervisory duties could be assigned to different authorities. However, because of the wide scope of due diligence and a large number of different sectors involved, decentralising the supervisory responsibilities would not necessarily make the supervision easier.[388] Designating the supervisory authority would also depend on the tasks that the authority is intended to perform. Supervising compliance with the reporting obligation would be easier than active supervision of due diligence.

If supervision is assigned to the authorities, the powers of the authorities concerned must also be determined. Should the authority organise the collection of information or would it also be given supervisory duties and the right to impose administrative sanctions? If it is decided to introduce a system in which compliance with the reporting obligation is supervised, the appropriate supervisory authority would vary depending on how the reporting is carried out. For example, the Finnish Patent and Registration Office could be the right government agency to supervise the reporting required in connection with the submitting of financial statements.[389] If it is decided that the reporting would be by means of a new centralised register, the party maintaining the register could also act as the supervisory authority. If companies are only obliged to publish the report on their websites or on a comparable platform, the main responsibility for supervision would lie with the companies' stakeholders. In this case, the supervisory authority or a court could have the powers to oblige the operator to comply with the reporting obligation. The act might also contain provisions allowing the authorities to enforce compliance with the obligation by means of a conditional fine.[390]

Provisions on any other powers granted to the authorities should also be laid down in the law. For example, the Timber Act allows the supervisory authorities to conduct inspections in an operator's premises and request information from the operator.[391] Similar powers are also proposed in the unofficial German legislative proposal.[392]

One key issue regarding official supervision concerns the objectives of and the need for such supervision. Large companies are already supervised by their stakeholders, whose

388 For example, supervising compliance with the Anti-Money Laundering Act is the responsibility of several authorities; Chapter 7, section 1 of the Anti-Money Laundering Act. However, in the Anti-Money Laundering Act, the supervisory tasks of the authorities cover a limited number of operators and specific operations.

389 The Finnish Patent and Registration Office supervises compliance with the companies' obligation to submit financial statements (Chapter 8, section 1, subsection 2 of the Accounting Act).

390 See section 4 of the Act on Conditional Fines (1113/1990).

391 Sections 5 and 6 of the Timber Act.

392 Germany, Section 12 of NaWKG.

supervision includes monitoring the responsibility and sustainability of the companies' operations and there are increasing requirements for investors and financial institutions to do the same. If the legislation would also be applied to SMEs, the official supervision of their operations should be assessed separately. Supervision based on the reporting obligation would be a financial burden on companies and possibly also on the authorities. It should therefore be determined whether supervision of SMEs would produce results that are commensurate with the resources required by the supervision and necessary for achieving the objectives of the act. Instead of supervision, the tasks of the authorities could be limited to providing enterprises with advice and guidance designed to increase awareness of the impacts of business operations on human rights and the environment and to promote due diligence in enterprises.

Supervision of due diligence in companies could be left to the stakeholders or to the authorities. Supervision by stakeholders could also be enhanced by obliging (some) companies to report on their operations.

Implementing supervision by the authorities would involve a number of different challenges, depending on the supervisory tasks given to the authorities and the scope of the act. Especially a combination of extensive supervisory duties and a wide scope of the act might make it difficult to organise the authorities' activities and to find the authorities suited for the task.

In addition to or instead of supervision, the tasks of the authorities could include the provision of due diligence advice and guidance for enterprises.

5.3.3.2 Remedial action and liability for damage

5.3.3.2.1 Remedial legal action

Under the UN Guiding Principles, companies should provide for or cooperate in remediation in situations in which they have caused or contributed to adverse impacts.[393] Issues concerning the introduction of remedial and compensation obligations (in particular, liability for damages) are briefly discussed below. The focus is on the scope of the obligation and on the burden of proof. This approach is based on the fact that tort liability is a wide-ranging subject, especially in transboundary situations, and it is not possible to exhaustively discuss all issues concerning damages and remedial action within the framework of this report. For example, the extensive issue of access to legal remedies and the potential need for any reform of the legal system[394] are outside the scope of this

393 Principle 22 of the UN Guiding Principles.

394 For example, the following factors may make it more difficult to seek compensation by legal means: right of action, access to legal aid, duration of proceedings, and legal costs; see Zerk 2011, pp. 65–78. Of the other means the state can use to ensure access to remedies, see DGEP 2019, p. 11.

report. Depending on the selected approach and if it is considered appropriate to hold companies legally liable for failing to exercise due diligence, a more detailed examination of questions related to the formulation and limitation of the liability may be called for.

Providing for remedies or cooperating in them is connected with the obligation of companies to prevent adverse human rights and environmental impacts arising from their operations. The rules governing companies' obligation or their opportunities to address adverse impacts arising from their operations could be laid down in the law.[395] For example, the unofficial German legislative proposal contains a provision explicitly obliging companies to take remedial action when they notice that they have caused or are about to cause adverse impacts.[396] The remedial actions may not always be adequate or companies may be unwilling to make them available. In such cases, the possibility to seek remedial action from judicial mechanisms provided by the state is in a key role.[397]

Compensation for damage is a key form of legal remedy and its aim is to share the adverse impacts arising from the damage between the injured party and the party causing the damage. In addition to the compensation effect (Finnish tort law recognizes restorative, not punitive compensation), liability for damages has a preventive impact: the threat of liability encourages the operator to organise its business in a manner that allows it to avoid liability.[398] Different types of damages are usually classified on the basis of where the adverse change occurs: in a person, object or property. Instead of having to pay a monetary compensation, the party causing the damage may also be obliged to redress the damage that it has caused.[399]

5.3.3.2.2 Scope of liability for damage

Existing legislation contain provisions, under which companies may be held liable for damages they have caused. Liability can be based on a contractual relationship or on the basis of general non-contractual liability for damages (tort law).[400] Imposing upon companies a liability for damages occurring in their supply chains would extend the existing liability of companies. If liability for damages caused by neglecting the due diligence obligation is introduced, the extent of the liability in a company's supply chain

395 For example, under sections 34 and 36 of the Sales of Goods Act (355/1987), the seller can remedy a defect and in the same connection, the buyer can require that the defect should be remedied.

396 Germany, Section 7 of NaWKG.

397 Principle 27 of the UN Guiding Principles; United Nations High Commissioner for Human Rights, *Improving accountability and access to remedy for victims of business-related human rights abuse through State-based non-judicial mechanisms*, A/HRC/38/20, p. 4.

398 Ståhlberg – Karhu 2013, pp. 27–28.

399 For example, the Act on the Remediation of Certain Environmental Damages (383/2009; Environmental Liability Act).

400 The Tort Liability Act (412/1974) is the general act laying down provisions on the compensation for damage. There are also provisions on the compensation for damage in a number of other acts.

should be determined. Holding a company liable for damages that are entirely beyond its control and/or damage that is difficult to anticipate would not be justified. The OECD Guidelines also draw attention to the fact that even though companies should work to prevent or mitigate the adverse impacts arising from their operations, the aim should not be to shift liability from the parties causing the impact to the companies in a business relationship with them.[401]

Under the French act on corporate social responsibility, a company's liability for damages applies to the damage caused by corporations under its control and its established business partners. If the failure to exercise due diligence leads to a situation in which any of the enterprises controlled by the company or any its business partners causes adverse human rights or environmental impacts, the liability of the parent company would be connected with its failure to exercise due diligence or meet its supervisory obligations.

Under the Swiss counter-proposal, a company would be liable for personal injuries and property damage caused by enterprises under its control. Liability for damages based on economic dependence is explicitly left outside the scope of the act. Thus, liability for damages would only apply to damage caused by the subsidiaries controlled by the company. In the proposal, the provision on liability for damages is placed in the section determining the employer's liabilities.[402]

Holding a company directly liable for the action of the enterprises under its control differs from the principle of separate liability of legal persons and from the principle that the party causing the harm is responsible for its reparation. There are a number of exceptions to this general rule and holding a company liable for the action taken by enterprises under its control is not entirely unknown in the Finnish legislation either. Under the Act on Compensation for Environmental Damage, in addition to the operator, the party that is comparable with the operator can also be held liable for the harm that has not been caused intentionally or negligently.[403] However, the view in literature is that this would require a relationship differing from a normal parent company-subsidiary relationship under company law.[404] In case law, deviating from the doctrine of separate legal personality (piercing the corporate veil) is also considered possible if certain clearly specified requirements are met. Thus, holding companies liable for the action of their subsidiaries is already possible under existing legislation in a small number of specific cases. Extending this liability in a manner that would make a company directly liable for

401 OECD Guidelines, II.A.12.

402 See Chapter 3, section 1 of the Tort Liability Act.

403 Section 7 of the Act on Compensation for Environmental Damage.

404 Hollo – Utter – Vihervuori 2018, pp. 287–288.

the actions of foreign-based enterprises under its control would deviate from the principle of legal person's separate liability and national case law.

Scope of the liability for damages is also limited by the general principles of tort law. For a company to be held liable for damage that has occurred in its supply chain would require that 1) damage has occurred; 2) there is negligence involved; 3) the damage suffered was caused by negligence (causal link); and 4) the damage was foreseeable. A company cannot be held liable for damages that are completely unanticipated in relation to its operations. The requirement for a causal link between negligence in the company's operations and the harm caused on the one hand and the predictability of the damage on the other would probably lead to a situation in which the company would not be held liable for harm, which is beyond its control or unanticipated.[405]

5.3.3.2.3 Due diligence and burden of proof

Both the French act on corporate social responsibility and the Swiss counter-proposal contain what is called due diligence defence. Under the defence, a company could be exonerated from its liability if it is able to show that it has exercised due diligence or that it has not been able to influence the operations of an enterprise under its control.[406] In terms of tort law, the issue concerns the assessment of negligence.

In situations involving compensation for damage, the injured party should thus show that a harm has occurred and that it has resulted from negligence. The causal link between negligence and the damage as well as the adequately foreseeable nature of the damage should also be demonstrated. Negligence can be defined as meaning the failure to exercise required care. The required level of care, as well as issues concerning the causal link and the foreseeable nature of the damage are determined on a case-by-case basis. The assessment of appropriate measures may take into account such factors as the likelihood and magnitude of the risk.[407] The due diligence or duty of care required under law would also have to be considered when the appropriateness of the actions of a company is determined.[408] Thus, the party presenting a claim for damages could show that a particular area of due diligence has been neglected; for example, the company has not conducted adequate risk assessments or has failed to take preventive measures to address identified risks. The reports and other information required of the company could serve as evidence in claims for damages.[409]

405 Pietropaoli et al. 2020, p. 47

406 France, Art. 225-102-5; Savorey 2020, pp. 68–69; Study on Due Diligence, pp. 193–194.

407 van Dam – Gregor 2017, p. 125; Savela 2015, pp. 59, 305–317.

408 See Hemmo 2003, p. 244.

409 There is some indication that corporate social responsibility reporting has increased the number of claims; Study on Due Diligence, p. 228.

In tort law the burden of proof lies primarily with the injured party, which should, among other things, be able to prove that the company has acted in a negligent manner. In legal literature, this approach has been considered problematic with regard to adverse human rights impacts. This is partially due to difficulty of proving causality and negligence, but also and because the injured party is often poorly placed to obtain information required for pursuing the claim from the companies.[410] Reversing the burden of proof has been proposed as a solution to ease the burden of the injured party.[411] The burden of proof could be reversed entirely or, for example, with regard to the causal link between the failure to meet the due diligence obligation and harm. Reversing of the burden of proof would also make it easier for the claimant to obtain the required information from the company.[412]

In Finland, reversing of the burden of proof is permitted, for example, under the Limited Liability Companies Act, under which a member of a company's management must demonstrate that they have exercised due care if the company has suffered harm through breaches of the Limited Liability Companies Act or the company's articles of association or through action for the benefit of a related party. It should be noted, however, that the reverse burden of proof is not applied in situations in which only the principles laid down in Chapter 1 of the Limited Liability Companies Act have been breached. These principles also include the general duty of care of the management. Considering the general nature of the principles, reversing the burden of proof was deemed an excessively harsh instrument when issues pertaining to the liability of the company's management are addressed.[413] The provisions on liability for damages contained in the Limited Liability Companies Act apply to harms suffered (asset losses incurred) by the company and, ultimately, by its shareholders. The need for legal protection concerning human rights and the environment can be considered substantial. If the burden of proof in claims for human rights and environmental damages is to be redistributed, the liability of the company (management) should be weighed against the protection of the injured party.

Strict liability may also be imposed on the operator, in which case negligence is not a consideration. An operator with strict liability cannot avoid its liability by acting with due care. Traditionally, provisions on strict liability apply to sectors involving a particularly high risk.[414] The principle of strict liability is also laid down in the Act on Compensation for Environmental Damage.[415] Bringing environmental damage within the scope of strict

410 Savorey 2020, pp. 68–69.

411 Switzerland, Art. 55, Art. 759a, Art. 981a.

412 DGEP 2019, p. 109.

413 Chapter 22, section 1, subsection 3 of the Limited Liability Companies Act.

414 Section 103 of the Mining Act (621/2011); Nuclear Liability Act (484/1972); section 3 of the Rail Traffic Liability Act (113/1999).

415 Section 7 of the Act on Compensation for Environmental Damage.

liability was justified by stating that in environmental pollution, it is usually difficult for the injured party to present evidence of negligence. This provision thus protects the injured party.[416] The Act on Compensation for Environmental Damage also eases the burden of proof of the injured party by only requiring a probable causal link between the operations and the damage.[417] This arrangement offers an alternative way of solving the same problems of evidence that can be addressed by reversing the burden of proof.

Applying strict liability would, however, deviate from the general principle of due care under which the operator may, by acting with care, avoid liability for damages. Introducing strict liability would significantly increase a company's liability and the risks associated with its foreign operations. Strict liability could also include a due diligence defence, that is the possibility of avoiding liability if the company could show that it has acted with care. In such cases, the legal assessment would resemble the evaluation carried out in connection with negligence liability except that the burden of proof would lie with the company.[418]

When considering the scope of the liability for damages and the sharing of the burden of proof, the doctrine of separate legal personality (a factor favouring a high threshold for compensation) can be set against the need to provide those in a vulnerable position with legal protection (a factor in favour of setting the threshold at relatively low level).

5.3.3.2.4 Damage to be compensated and other issues

In many cases, environmental pollution or other environmental damage also causes personal injuries or property damage. Direct environmental damage does not always fit into this definition. Under the Swiss counter-proposal, compensation for damage would only be paid for personal injuries and property damage. No compensation would be paid for damage that only affects the environment. A similar solution is also conceivable in Finland. The French act on corporate social responsibility and the unofficial German legislative proposal do not leave damage that only affects the environment outside the scope of the compensation (at least not explicitly). Under the Environmental Liability Directive of the EU, a restoration responsibility may be imposed on the party causing the damage, which means that the operator might be obliged to take remedial action instead of having to pay financial compensation.[419] The remedial action set out in the Environmental Liability Directive is based on the measures determined by the

416 Hollo et al. 2018 pp. 253–254.

417 Section 3 of the Act on Compensation for Environmental Damage.

418 See van Dam 2013, pp. 302–306.

419 Directive 2004/35/CE of the European Parliament and of the Council on environmental liability with regard to the prevention and remedying of environmental damage (Environmental Liability Directive). The directive has been implemented in Finland by enacting the Environmental Liability Act and by amending other environmental laws.

authorities.[420] Implementing similar arrangements in international scale would probably involve problems that should be assessed separately.

Liability for damages could also be left out of any corporate social responsibility legislation, at least in the first stage of the legislation. This would give companies time to adapt to the new requirements. The provision could be added to the act if necessary and as more legislative experience is accumulated. The weakness of this solution would be that in the absence of liability for damage, there would no new opportunities for victims to access legal remedies, which has been considered as one aim of the regulation.

The liability for damages imposed on companies for failing to exercise due diligence would provide parties suffering damage as a result of the companies' operations a chance to receive compensation.

With regard to compensation, the scope of the statutory liability should be considered. Under the UN Guiding Principles, a company must provide for or cooperate in remediation when causing adverse impacts or contributing to them. Statutory liability for damages could be limited to a company and enterprises under its control.

Under tort law, the injured party must show that damage has been caused, that the party causing the damage has shown negligence and that there is a causal link between the negligence and the damage. The burden of proof placed on the injured party has been considered to hamper access to remedies. When the reversal of the burden of proof or other ways of easing the burden of proof are examined, consideration should be given to the consequences of extending the scope of a company's liability and the need of the injured party for legal protection.

5.3.3.3 International liability for damage

Before a possible infringement taking place in the territory of another country is brought before a court, issues concerning jurisdiction and applicable laws must be addressed. The Brussels I Regulation contains provisions on the jurisdiction of courts in civil and commercial matters in the European Union. Under the regulation, action against an individual domiciled in an EU Member State must be brought in a court in the Member State in question.[421] The regulation also applies to legal persons, such as companies, whose operating location is determined on the basis of their statutory seat, central administration or principal place of business. Under the regulation, an action for damages against a Finnish company could be brought in Finland.[422]

420 Environmental Liability Act.

421 Regulation (EU) No 1215/2012 of the European Parliament and of the Council on jurisdiction and the recognition and enforcement of judgements in civil and commercial matters (recast) (Brussels I Regulation).

422 TEM 14/2015, p. 28–29.

The Rome II Regulation plays a key role in the international conflict of laws. The regulation contains provisions on the law applied to non-contractual obligations.[423] Under the general rule of the regulation, the applicable law is the law of the country 1) in which the damage occurs, irrespective of the country in which the event giving rise to the damage occurred; 2) in which the person claimed to be liable and the person sustaining the damage have their habitual residence; 3) which is manifestly more closely connected with the event than the countries referred to above.[424] In the case of environmental damage, the injured party may base their action on the law of the country in which the event giving rise to the damage has occurred.[425] Under the regulation, Finnish law would not, as a rule, be applicable to damage occurring in another country.[426]

However, exceptions to the general rule can be made under the Rome II Regulation on the basis of overriding mandatory provisions.[427] Such provisions can be applied regardless of the law that would otherwise apply. It has been suggested in legal literature that the statutory due diligence obligation and the conflict of laws provision that might be incorporated into it could allow exceptions to the general rule of the Rome II Regulation.[428] Both the Swiss counter-proposal and the unofficial German legislative proposal contain a conflict of laws provision under which the act could also be applied in situations in which applying international conflict of laws provisions could lead to a different interpretation.[429] A similar provision could also be included in the Finnish act on corporate social responsibility.

Actions concerning transboundary operations also involve issues pertaining to conflict of laws with regard to international private law. A provision laying down the applicable law could be included in the legislation.

423 Regulation (EC) No 864/2007 of the European Parliament and of the Council on the law applicable to non-contractual obligations (Rome II Regulation).

424 Article 4 of the Rome II Regulation.

425 Article 7 of the Rome II Regulation.

426 Environment damage defined in the regulation are a possible exception; see Enneking 2017, pp. 51–53.

427 Article 16 of the Rome II Regulation.

428 Lautjärvi 2019, p. 442; Enneking 2017, pp. 55–57; TEM 14/2015, pp. 29–30.

429 Switzerland, Article 139a of the Federal Act on Private International Law; Germany, Section 15 of NaWKG.

5.3.3.4 Administrative and criminal sanctions

Failure to comply with the statutory obligations could also lead to administrative sanctions, punitive administrative sanctions or criminal sanctions. The purpose of administrative sanctions is to establish or restore the legal state of affairs. In corporate social responsibility legislation this could be in the form of a conditional fine, the aim of which is to ensure that the companies meet their reporting obligation. Punitive administrative sanctions, on the other hand, can be compared with criminal sanctions.[430]

Both environmental and human rights offences are already criminalised under the Finnish Criminal Code. Under Finnish law, both natural and legal persons can also be held criminally liable for offences committed outside Finland in certain cases. This usually requires a connection between the offence and Finland, and in most cases, the offence must also by punishable under local law. The Criminal Code also lists criminalised acts, in which Finnish law can be applied irrespective of local law. Such offences include human trafficking and aggravated human trafficking. [431] Cross-border criminalisation of international business operations is outside the scope of this report. From the perspective of the corporate social responsibility legislation examined in this report, the administrative or criminal sanctions would be applied if a company under Finnish jurisdiction fails to exercise due diligence or to comply with due diligence reporting obligations.

The legal enforcement and supervisory methods should be proportionate to the seriousness of the offence and other relevant factors. When sanctions are considered, it should be assessed whether the intended objectives could be achieved by less stringent means or by applying other administrative sanctions. The nature of the act or negligence concerned and the relationship between the proposed sanction and other administrative and criminal sanctions should be examined in the assessment. Administrative sanctions are considered particularly well-suited for relatively minor offences and acts of negligence, in which there is clear evidence of non-compliance with the statutory obligations. Criminal sanctions should only be used as the last-resort measure, if the intended results cannot be achieved by other means.[432] This consideration should also be applied to any corporate social responsibility legislation after its scope and content have been determined.

Administrative sanctions can be imposed on natural and legal persons and the penalty fees can be staggered so that harsher sanctions are imposed on aggravated forms of violations.[433] Administrative sanctions are imposed by administrative authorities. Competence is usually allocated to an authority that is best placed to determine the

430 See OM 52/2018, pp. 20-23.

431 See Chapter 1, sections 7, 8 and 9 of the Criminal Code; HE 1/1996, pp. 4–5; TEM 14/2015, pp. 39–41.

432 OM 52/2018, pp. 24-25.

433 Of the possible overall assessment of the penalty fee, see for example, section 41, subsection 2 of the Act on the Financial Supervisory Authority (878/2008).

sanctions criteria and that possesses the expertise required for that. In some cases, it has been considered appropriate to allocate the responsibility for imposing substantial penalty fees to multi-member bodies.[434] With regard to administrative sanctions, it should therefore be considered which authorities would be best placed to supervise corporate social responsibility. Particular consideration should be given to the challenges arising from the supervision of an extensive obligation.

There are already legal provisions under which criminal sanctions can be imposed on companies failing to comply with their reporting obligations. For example, fines or more severe penalties can be imposed on companies for not complying with the obligation to prepare financial statements or for neglecting their reporting obligations.[435] A conditional fine or, if the act is intentional or involves gross negligence, criminal sanctions can be imposed for not complying with the annual reporting obligation laid down in the Extractive Industries Act.[436] Imposing sanctions for non-compliance with a reporting obligation would also limit the scope of the sanctions, especially if the scope of the statutory reporting obligation would only apply to a number of enterprises.

The Dutch act contains provisions on criminal sanctions for non-compliance with the due diligence obligation. Under the act, the company's management can be held criminally liable in a situation in which administrative sanctions have been imposed on the company for non-compliance with the reporting or due diligence obligation and the offence is repeated within five (5) years of the imposition of the administrative sanctions.[437] Under the unofficial German legislative proposal, a company's compliance officer could be held criminally liable.[438]

Under the Finnish Timber Act, enacted to implement the Timber Regulation, **intentional** non-compliance with the due diligence system referred to in Article 4 of the Timber Regulation is a punishable offence.[439] It was determined in the preparatory work of the act that administrative sanctions (for example, a temporary ban on placing products on the market) would not be an efficient way to address situations in which non-compliance with the obligation is continuous and intentional. Non-compliance could be considered intentional if there is a complete lack of a due diligence system or in a situation in which

434 For example, the decisions on the administrative penalty fees payable under the General Data Protection Regulation are made by the Sanctions Board; Data Protection Act (1050/2018); see also OM 52/2018, p. 37.

435 See Chapter, 8, section 4, subsection 1, paragraph 4 of the Accounting Act; Chapter 30, sections 9 and 10 of the Criminal Code.

436 Section 8, subsection 3 and section 9 of the Extractive Industries Act.

437 The Netherlands, Art. 9.

438 Germany, Section 14 of NaWKG.

439 Section 12, subsection 2 of the Timber Act. The due diligence system referred to in Article 4(2) of the Timber Regulation is described in more detail in Article 6 of the regulation.

key elements of due diligence are absent.[440] Imposing sanctions for non-compliance with the due diligence obligation involves case-by-case assessment and violations are not necessarily easy to prove. In such cases, from the perspective of the investigative powers and the legal protection of the company, there are good grounds for criminal liability, where it is for a court to carry out the assessment.[441]

The principle of legality under criminal law contains the prohibition to introduce criminalisations that are too extensive and **vague** in terms of their essential elements. The purpose is to ensure that everybody is in a position to understand what is prohibited under criminal law. For example, open descriptions of prohibited actions are considered legislatively problematic and they should be interpreted in a narrow manner.[442] The fines clause contained in the French act on the due diligence obligation has also been repealed because the obligation was considered to be too vague in terms of criminal law.[443] The due diligence system laid down in the Timber Regulation and its content are relatively detailed and apply to a specific activity.[444] Moreover, it is stated in the preparatory material for the Timber Act that criminal sanctions are preceded by a written request and an order to correct any inadequacies of the due diligence system.[445]

Depending on the content of the due diligence provision, a similar penal provision concerning due diligence would, in terms of its essential elements, be vaguer than the penal provision of the Timber Act, for the simple reason that due diligence is intended to cover both human rights and the environment. It is, however, conceivable that **intentional** non-compliance with the due diligence obligation could be made a criminal offence. In that case, intent could, in the same manner as in the Timber Act, be connected with the complete absence of due diligence or its key elements (such as impact assessment).[446] It should also be considered whether there is a need for requests and orders by the supervisory authority that would precede criminal sanctions and clarify the content of the required measures to the operator.

In Finland, a corporation, foundation or other legal person in the operations of which an offence has been committed can be sentenced to a corporate fine if the corporate fine is explicitly included as a sanction for the offence.[447] The forfeiture sanctions for offences

440 HE 97/2013 vp. p. 16.

441 See OM 52/2018, pp. 25–26.

442 Tapani et al. 2019, pp. 131–133.

443 Savorey 2020, p. 72.

444 Article 6 of the Timber Regulation.

445 HE 97/2013 vp., p. 28. Section 8 and section 9, subsection 1 of the Timber Act.

446 Of the assessment of negligence under criminal law in general, see Lappi-Seppälä et al. 2013, pp. 173–176.

447 Chapter 9 of the Criminal Code. In Italy, a legal person may defend itself against charges for certain offences by showing that it has taken adequate measures to prevent the offences; Study on Due Diligence, pp. 171–172; Ruggiero 2016.

could also be considered, for example, in cases in which child labour has been used in the manufacturing of the products.[448]

Administrative and criminal sanctions, could also be added to the act at a later stage, when it has been applied in practice, first assessments of its impacts are available and when companies have had enough time to adapt to the requirements of the new legislation.[449] The need for a phased introduction of the legislation may depend on such matters as its scope: if the act applies to a large number of enterprises that are completely unfamiliar with corporate social responsibility issues, there are more grounds for providing enough time for adaptation than in cases in which the act is only applied to companies that are already obliged to submit responsibility reports.

Administrative or criminal sanctions could also be imposed for non-compliance with the due diligence obligation. When the sanctions are imposed, the objectionable nature of the act in question and the prospect of achieving the intended results by other means should be assessed. Sanctions could concern at least non-compliance with the reporting obligation imposed on the company.

5.4 Regulatory approaches

The due diligence obligation could be introduced by enacting a separate act, by amending existing legislation or by a combination of the two approaches. In the reference countries discussed in this report, due diligence provisions have been introduced by enacting a separate act[450] and by amending existing national legislation (such as corporate legislation).[451]

When implementing the reporting legislation introduced in the European Union, Finland has enacted separate acts and amended existing legislation.[452] There is a separate act on the disclosure of fees paid to the authorities by companies engaged in extractive industries and timber harvesting in primeval forests. At EU level, the obligation is laid

448 Chapter 10 of the Criminal Code.

449 Phased introduction of the sanctions is recommended in the report assessing the *Modern Slavery Act* of the United Kingdom; Independent Review of the Modern Slavery Act 2015, p. 46. Of the same approach to the French legislation, see Savorey 2020, pp. 78–79.

450 For example, The *Modern Slavery Acts* of the United Kingdom and Australia, and the Dutch act on child labour.

451 For example, The French act on due diligence, which amends the country's trade legislation (*Code de commerce)*.

452 Extractive Industries Act.

down in the Financial Statements Directive. In the Government proposal, the reporting obligation was, however, considered to be of different nature than the provisions on the financial position and profits of a party obliged to keep accounts and for this reason it was decided to enact a separate act.[453] However, in the case of the provision regulating NFI reporting a decision was made to include them in the Accounting Act.[454] This was prompted by amendments to the Accounting Act limiting the obligation to audit the management report. The view was that the easing of the audit obligation would make it possible to regulate NFI information in the Accounting Act. Regulation under the Securities Markets Act, Act on Credit Institutions and the Insurance Companies Act was mentioned as an alternative in the legislative history.[455] The due diligence obligation laid down in the Timber Regulation was implemented in Finland by a separate act.[456]

There are provisions on the regulation of businesses and their operations in a large number of Finnish acts. Incorporating provisions on the due diligence obligation in corporate legislation would require changes in a number of acts on different company forms that already contain provisions on the duty of care of management, liability for damages and supervision. Various duty of care obligations applying to enterprises are also laid down in a range of different acts, broken down in accordance with their object of protection. Provisions on human rights and the environment are also contained in a number of different acts. None of the existing acts explicitly covers both the protection of human rights and the environment. When imposing a new due diligence obligation that covers both human rights and the environment on businesses, it is particularly appropriate, from the perspective of comprehensibility and clarity of the legislative framework, to examine the option of introducing due diligence provisions in the form of a separate act.

In Finland, there are a number of acts containing provisions on companies' reporting and duty of care obligations. Enacting a new due diligence obligation covering both human rights and the environment in the form of a separate act could be the best option from the perspective of the comprehensibility of the regulation.

453 HE 89/2015 vp. p. 11.

454 Chapter 3 a of the Accounting Act.

455 HE 208/2016 vp, pp. 5–6; HE 70/2016 vp., pp. 12–13.

456 Timber Act.

6 Issues to be considered in legislative impact assessment

6.1 Impacts on enterprises

6.1.1 Costs incurred by enterprises

A due diligence obligation imposed on companies may have a variety of impacts, of which the impacts on companies, their stakeholders, the authorities and human rights and the environment should be considered in the legislative drafting. No proposal has been presented yet, and thus it is impossible to give any detailed assessment of its impacts. For this reason, the observations below only concern the factors that should be taken into account in an impact assessment of any government proposal, while at the same time, preliminary estimates of the impacts of the legislative solutions are also presented. It should be noted that while estimates of the costs arising from the obligations imposed on companies are available, few estimates on the impacts of the due diligence obligation on human rights and the environment are available as laws regulating these matters have only recently been introduced.

Companies incur costs as a result of the obligations imposed on them. With regard to cost estimates, it should be noted that they are influenced by a variety of different factors, which must be addressed during the legislative drafting. Costs may result from the establishment and maintenance of the due diligence process required under the regulation. The costs incurred by companies could comprise the labour costs allocated to the process or the costs arising from the use of outside experts.

Depending on the scope of the act, the costs may only affect a small number of large companies or companies operating in sectors considered to involve high risks or an extremely large number of companies. The costs arising from the act also depend on whether companies are required to exercise due diligence throughout their supply chains or only in the enterprises under their control and in the first-tier subcontractors. The costs

would also be impacted by a solution in which the reporting obligation imposed on the companies is of more limited scope than the rest of the due diligence obligation.

If the emphasis is put on the appropriateness of the duty of care, the costs incurred by companies would vary, depending on the type of their operations and company size. For small companies operating in low-risk sectors, the costs arising from due diligence could be very low. At the same time, for large international companies, the costs might be substantial.[457] If it is decided to apply due diligence with a specific content, the cost impact on SMEs would, in relative terms, probably be more substantial than on large companies with higher net sales.[458]

The measures that companies would be required to take to implement due diligence also generate costs. The obligation of the companies to set up a grievance mechanism, provide training, appoint an internal supervisor or use outside experts in the supervision would mean more costs for companies. Small companies in particular might incur substantial costs for having to use outside experts, to introduce internal management systems, and to appoint officials responsible for ensuring compliance with the provisions.[459]

In addition to generating costs, responsible corporate operations can also be considered to produce benefits for businesses. Estimating the financial value of these benefits is more difficult than assessing the costs. This is mainly because better financial performance is a sum of many factors and it is difficult to estimate the contribution of sustainability investments to the improvements. It has been suggested, however, that exercising due diligence may generate benefits for companies in the following sectors: company's reputation/brand, access to financing, market value, consumer trust and enhanced risk management.[460] However, assessing the benefits reaped by companies as a result of due diligence is not a key factor when corporate social responsibility legislation is considered. If a company concludes that exercising due diligence is economically profitable, it will also adopt responsible practices without legislation.

457 For example, see the estimates of workdays spent on due diligence in companies with more than 1,000 employees; Study on Due Diligence, p. 408.

458 See also the cost estimate concerning the Conflict Minerals Regulation applicable to SMEs; SWD(2014) 53, p. 47.

459 However, there is also a lightweight version of the EMAS eco-management and audit scheme, which is intended for SMEs; see EMAS 'easy' for small and medium-sized enterprises (available: https://op.europa.eu/s/n6iK).

460 Study on Due Diligence, pp. 301–315.

6.1.2 Impacts on competition

One key aim in the regulation of corporate human rights and environmental responsibility is to tackle the regulatory gaps arising from global supply chains and to regulate multinational business operations. In a global economy, Finnish companies operate in the same markets with companies from different parts of the world that observe their own national legislation. For this reason, the operating prerequisites of Finnish companies should also be kept in mind when the impacts of the corporate social responsibility legislation are assessed.

In enacted legislation, the due diligence obligation only applies to the protection of specific legal interests or large companies. Moreover, as the legislation only applies to the companies based in the countries concerned or operating in them, multinational companies may have to apply a wide range of different due diligence standards or submit reports describing same matters in different ways in different countries.[461] From the perspective of responsible corporate operations, the threat is that the varying content and scope of national requirements will lead to point solutions that may hinder the introduction of comprehensive environmental and human rights processes.[462]

National legislation also impacts the competitive environment of business enterprises. Depending on the content of the regulation, national legislation could require that Finnish companies and Finnish-based companies to adopt higher standards than, for example, companies operating in comparable European countries. The question whether the due diligence obligation is a competitive advantage or disadvantage is a different issue altogether. A common view is that responsible corporate operations give companies a competitive edge.[463] At the same time, however, additional legislation can be perceived as a competitive disadvantage that could increase operating costs in relation to other comparable countries. As business decisions on operations and locations depend on a wide range of different factors, the assessment of the impacts of a single act would require a comprehensive impact assessment before legislative measures are taken.[464]

461 The increased fragmentation of the EU single market was seen as a threat in the impact assessment of the Conflict Minerals Regulation, SWD (2014) 53, p. 29.

462 Study on Due Diligence,pp. 225–227, 239–240.

463 For example, COM(2011) 681, p. 12.

464 According to a questionnaire survey, the Bribery Act of the United Kingdom has not generated any major competitive advantages or disadvantages; Pietropaoli et al. 2020, p. 17. Assessing competitive effects is also connected with the academic debate on regulatory competition, in which it is suggested that freedom of location will lead to a 'race to bottom', in which companies seek to set up operations in the most permissive jurisdictions. The second option is the 'race to the top' in which legal certainty based on such factors as strict legislation would attract companies and increase investments. See for example, Gerner-Beuerle – Schillig 2019, pp. 115–116; Sjåfjell 2009, pp. 258–260.

In 2017, Finnish companies had 5,070 subsidiaries in 142 different countries.[465] More than 50% of the foreign net sales of Finnish companies were generated in the EU (excluding Finland). North America accounted for about 15% of the total.[466] Finnish corporate groups generate a relatively large proportion of their net sales in areas where human rights and environmental legislation has been introduced. However, net sales do not give an accurate description of the subcontractor chains of Finnish companies. At the same time, it should be remembered that the chances of companies to influence their supply chains vary from company to company. A report examining human rights actions brought against European companies in third countries does not list cases brought against Finnish enterprises. Likewise, only a small number of cases have been brought before the OECD National Contact Point in Finland.[467]

Both the existing reporting obligations and the due diligence practices voluntarily applied by companies have been criticised as insufficient to protect human rights and the environment.[468] When national legislation is considered, other regulatory projects under way, especially the EU debate on the regulation of due diligence, would also have to be examined. EU-level legislation would harmonise the laws of the Member States and the operating principles of the EU-based companies.[469] It was also highlighted in an EU-level stakeholder interview that a global problem needs a global solution.[470]

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465 Under Chapter 1, section 5 of the Accounting Act, a subsidiary is a company in which a Finnish company exercises control

- by having more than half of the voting rights based on the shares of the object company;
- by having the right to appoint or dismiss the majority of the members of the object company's board or similar body; or
- by having actual control over the object company in any other way.

466 Finnish enterprises' turnover abroad in 2017.

467 DGEP 2019, pp. 18–19; 31–32.

468 Of the inadequacies in due diligence, see for example, the UN Working Group on the issue of human rights and transnational corporations and other business enterprises, A/73/163 (16 July 2018), section 25. Of the inadequacies in reporting obligations, see Study on Due Diligence, p. 220 and the studies referred to in the publication.

469 Study on Due Diligence, pp. 142-147.

470 Study on Due Diligence, pp. 147-148. See also Sjåfjell et al. 2019, pp. 10–11.

6.2 Impacts on human rights and the environment

The positive human rights and environmental impacts created by a statutory due diligence obligation are estimated to be more substantial than those arising from voluntary guidelines and reporting obligations. However, the positive impacts will only materialise if companies carry out the risk assessments required for due diligence and comply with the regulation, which in turn requires effective enforcement of the legislation. At the same time, a poorly prepared or enforced piece of legislation would generate fewer positive impacts.[471]

In the field of human rights and the environment, the impacts of a due diligence obligation would be linked with ensuring that the company exercising due diligence would better supervise its supply chains and require that its contractual partners operating in countries with a lower level of human rights and environmental protection apply certain standards.[472] In other words, the impact is based on an assumption that the due diligence required by legislation will also flow through the requirements set by companies into other countries and enterprises across the supply chain.[473] For example, the due diligence obligation laid down in the Dutch act on child labour can be met by purchasing products and services from companies that have pledged not to use child labour. It has been suggested that this will lead to a situation in which there would only be business activities between partners/suppliers that have given such a pledge. Thus, the requirements of the act would pass through the supply chain.[474] This would also be in line with the UN Guiding Principles, under which companies should endeavour to address their human rights impacts using their leverage.[475] Local communities may also be negatively affected if, as a result of stricter legislation, companies decide, to reduce investments in areas or sectors that they consider particularly risk-prone.[476]

The environmental and the human rights impacts of the act might also vary depending on how many companies would fall within its scope. It is difficult to estimate how a due diligence obligation imposed on Finnish companies would impact developments outside Finland through supply chains.

471 Study on Due Diligence, p. 525.

472 Study on Due Diligence, pp. 510–511, 535–536.

473 See SWD(2014) 53, p. 56, which provides estimates of the indirect impacts of the Conflict Minerals Regulation.

474 Enneking 2020, p. 176.

475 Principle 19 of the UN Guiding Principles.

476 According to the questionnaire on the Bribery Act of the United Kingdom, there is some indication that companies have reduced investments in areas considered risk-prone; Pietropaoli et al. 2020, p. 17.

6.3 Impacts on consumers and investors

Due diligence exercised by companies has a consumer protection dimension. One aim of the legislation would be to provide consumers with information that they need when making purchasing decisions.[477] The due diligence obligation imposed on companies, and any reporting obligation attached to it, could thus make it easier for consumers to assess the level of corporate responsibility. It has also been noted that, for example, the due diligence obligation set in the Timber Regulation has made consumers more aware of the problems connected with illegal timber trade.[478] At the same time, the costs and any changes in the supply chains arising from the meeting of the due diligence obligation could, at least in theory, also be passed on to consumer prices.

Likewise, an increase in information on business operations and the human rights and environmental risks involved in it would make it easier for investors to assess the risks associated with companies' operations and thus facilitate investments in sustainable and responsible business operations.

6.4 Impacts on authorities' work

The impacts of any legislation on the work of the authorities depend entirely on contents of the act. Official supervision requires resources. The extent of the required resourcing depends on such factors as the number of companies to be supervised and the tasks given to the authorities. Providing recommendations and advice requires fewer resources than continuous supervision. Also, carrying out any reporting obligation within the framework of an existing information systems would require fewer resources than developing a completely new system.

477 The purpose of protecting consumers is clearly stated in the Californian act (sec. 2) but it is also a factor behind the Dutch due diligence act on the use of child labour.

478 Study on Due Diligence, p. 253.

7 Summary

7.1 Key questions

This report has examined the possibility of introducing in Finland a corporate due diligence obligation concerning human rights and the environment in accordance with the UN Guiding Principles and the OECD Guidelines.

Due diligence

Companies exercising due diligence should 1) identify and assess the impacts of their operations on human rights and the environment; 2) prevent and mitigate identified adverse impacts, 3) monitor the effectiveness of their measures; and 4) communicate on them. Due diligence is a risk-based approach and different companies can meet the obligation in different ways. Companies should identify and prioritise the most important risks to human rights and the environment arising from their operations.

Due diligence described in the UN Guiding Principles and the OECD Guidelines resembles duties of care found in national legislation. Duty of care usually refers to an obligation to exercise appropriate care to prevent a specific risk. Correspondingly, due diligence in human rights and environmental matters would oblige companies to prevent risks to human rights and the environment arising from their operations. Due diligence does not oblige the parties concerned to achieve a specific end result. Thus, the realisation of operational risks does not automatically mean that the obligation to exercise due diligence had been neglected.

Due diligence is context-specific and the actions that operators are required to take may vary. Identifying and preventing adverse human rights and environmental impacts are the key elements of due diligence. As a rule, companies decide themselves how they identify and prevent risks arising from their operations. Legislation could also oblige companies to implement specific measures intended to ensure due diligence.

If an obligation to exercise due diligence is introduced, the due diligence obligation could be described in general terms emphasising the appropriateness and proportionality of the obligation. Alternatively, the actions required for exercising due diligence could be defined as precisely as possible. When different options are examined, consideration should be given to such issues as legal certainty of companies, the need for legal protection of human rights and the environment, and the number of companies falling within the scope of the envisaged legislation.

The purpose of a disclosure obligation related to due diligence is to allow stakeholders and the authorities to assess the operations of the company. Under enacted laws, companies are usually required to meet their disclosure obligations by submitting reports on their approach to human rights and the environment. A disclosure obligation requires companies to allocate resources to producing the reports and for this reason, the reporting obligation could be more limited in scope than the rest of the due diligence obligation. One option could be to introduce a reporting obligation that only applies to the largest companies.

Definitions

The question of what legal interests should be protected is a key issue in the envisaged legislation. Defining the object of protection is also important to ensure legal certainty of companies. Human rights are defined in international agreements. The concept of the environment can be defined in different ways and the environmental impacts coming within the scope of legislation can be roughly divided in two categories: 1) those with bearing on human rights; and 2) those with bearing on the environment only. From the perspective of applying and interpreting the law, relevance should also be attached to the qualifiers that may be added to human rights and environmental impacts, such as **serious, significant** or **essential**, which limit the scope of the act. The appropriateness of these additional qualifiers should be assessed separately for human rights and the environment.

Scope of application

In many cases, the existing and proposed due diligence legislation only applies to companies of specific size or companies operating in specific sectors or specific geographical areas. Similar limitations to the scope of application should also be considered in Finland.

A risk-specific scope of application based on operating sectors or areas could be linked to other limitations by for example, imposing a due diligence obligation on large companies, and companies operating in particularly high-risk sectors. Any limitation to the scope of the law could also only apply to certain parts of the due diligence obligation (such as reporting).

Finnish legislation applies to the operations of companies registered in Finland and companies operating in Finland. By obliging Finnish companies to exercise due diligence in their supply chains, the impact of the legislation could be extended outside Finland's borders. It would also have to be decided how far in their supply chains companies should comply with this obligation. Due diligence could apply to the entire supply chain or be limited to the enterprises controlled by the company. Due diligence extending throughout the entire supply chain would be limited by the appropriateness and proportionality of the requirement: companies would not be required to show the same level of awareness of the impacts of their operations or to take uniform action in all parts of their supply chains. Moreover, the obligation of the companies to provide for or cooperate in remediation for the adverse environmental and human rights impacts of their operations could be more limited in scope than their obligation to exercise care.

Supervision

Supervision ensuring that companies exercise due diligence in in their operations could be left to their stakeholders or assigned to the authorities. Supervision by stakeholders could also be promoted by obliging (some) companies to report on their operations.

Supervision by the authorities would involve a number of different challenges, depending on the supervisory tasks given to the authorities and the scope of the act. In particular, extensive supervisory duties and/or a wide scope of the act would make it difficult to organise supervision and to find the authorities best suited for the task. In addition to or instead of supervision, the tasks of the authorities could include the provision of due diligence advice and guidance for companies.

Compensation for damages, and administrative and criminal sanctions

The liability for damages imposed on companies for failing to exercise due diligence would provide parties suffering damage as a result of the companies' operations a chance to receive compensation. Liability for damages would apply to damage arising from the failure of the company to exercise due diligence: for example, from the failure of a company to take appropriate measures to identify risks associated with its operations or to prevent identified risks. Under the UN Guiding Principles, a company must provide for or cooperate in remediation when causing adverse impacts or contributing to them. In the envisaged legislation, liability for damage could be limited to the company itself and the enterprises under its control.

Under tort law, the injured party must show that damage has been caused, that the party causing the damage has shown negligence and that there is a causal link between the negligence and the damage. The burden of proof has been considered to hamper access

to remedy. When the reversal of the burden of proof or other ways of easing the burden of proof are weighed, consideration should be given to the consequences of extending the scope of a company's liability and the need of the injured party for legal protection.

Claims in transboundary operations involve conflict of laws issues pertaining to international private law. The conflict of laws provisions might lead to situation in which it would be difficult to bring a claim for damages against a Finnish company as a result of damage occurring in another country. Some of the issues concerning the conflict of laws could be solved by means of a provision specifying the applicable law.

Administrative or criminal sanctions could also be imposed for non-compliance with the due diligence obligation. The sanctions on companies could apply to non-compliance with the reporting obligation. When the sanctions are imposed, the objectionable nature of the act in question and the prospect of achieving the intended results by other means should be assessed.

Regulatory method

There are a number of acts in Finland containing provisions on corporate reporting and duty of care obligations. If it is decided to introduce a new due diligence obligation covering both human rights and the environment, enacting a separate act could be the best option in terms of the comprehensibility of the legislation.

Companies are still relatively unfamiliar with human rights and environmental due diligence. Phased introduction of the statutory obligations and sanctions would give companies time to adapt to the new requirements. Guidelines and advice could also play an important role in increasing understanding and awareness of the theme among companies and it could serve as an element complementing an act on corporate social responsibility.

7.2 Tabular summary

The table below presents a number of identified factors that should be considered if a corporate due diligence obligation is introduced in Finland. The following themes are described in the table on general level: Object of due diligence, scope of application, dimension of due diligence in the supply chain, content of due diligence, reporting, supervision, liability for damage, and sanctions.

	Options	Estimate
Object of due diligence	Human rights and the environment	• Obligation giving extensive consideration to social impacts of business operations.
	Human rights, and the environment as part of human rights	• Addressing environmental impacts as part of human rights would put due diligence focus on cases in which the injured party can be identified. • The solution would narrow the scope of legislation and the protection provided by it.
	Serious human rights and environmental impacts	• Limiting due diligence to serious human rights and environmental impacts would encourage companies to exercise due diligence in the most serious violations. • The protection provided by the legislation would be narrowed.
Scope of application	All enterprises	• Broad scope of application would require that emphasis in the legislation is on the appropriateness and context-specific nature of due diligence. • It is conceivable that certain obligations, such as the reporting obligation, could only apply to specific companies.
	Large enterprises and SMEs	• Leaving out micro-enterprises would substantially narrow the scope of application.
	Large enterprises	• The act would only apply to a small number of companies. • The act would apply to companies that already have the largest number of obligations.
	Risk-based or geographical scope of application	• This would require the definition of high-risk sectors and/or areas of operations.
	Different obligations for different areas of application	• Different areas of application could be set for different statutory obligations. For example, a due diligence obligation applying to all companies and a reporting obligation only applying to large enterprises.
Scope of due diligence in the supply chain	Supply chain as a whole	• Due diligence applying to the entire supply chain would emphasise the appropriateness of due diligence. Due diligence would not be applied in the same way to enterprises controlled by the company and to parties way up in the supply chain.
	Enterprises controlled by a company	• Limiting the scope of due diligence to enterprises under a company's control puts the due diligence focus on areas where the company is best-placed to exert influence. • Leaving other adverse impacts occurring elsewhere in the supply chain outside the scope of due diligence would weaken the protection provided by the legislation.
Content of due diligence	General obligation to exercise due care to prevent adverse human rights and environmental impacts	• Formulating the due diligence obligation as a general obligation would emphasise the context-specific nature of due diligence. • Linking due diligence legislation to processes of the UN and the OECD would help to specify the actions required for due diligence. • Additional guidance could be provided to enhance corporate awareness and understanding of due diligence and the impacts of business operations on human rights and the environment.
	Detailed provision laying down the content of the due diligence obligation	• A detailed provision on the content of the due diligence obligation might weaken the appropriateness of due diligence. • Detailed requirements might require more resources from enterprises.

	Options	Estimate
Reporting	No reporting obligation	• Enterprises are not obliged to provide stakeholders with information on compliance with due diligence obligation, which would make it more difficult for stakeholders to supervise operations.
	Reporting obligation	• Specifying the content of reporting would enhance the comparability of the information supplied to the stakeholders. • Detailed reporting obligation could be limited to the largest companies.
Supervision	No official supervision	• Supervision of companies by stakeholders could be supported by requiring companies to publish information on the adverse impacts of their operations and on the action that they have taken to prevent them.
	Official supervision	• Supervision could be directed at reporting by the company and/or due diligence. • A suitable supervisory authority should be determined as part of the legislative process. • Official supervision can be combined with providing guidelines and advice, which would make companies more aware of the human rights and environmental impacts of business operations and of due diligence.
Liability for damages	Scope of liability for damage	• Because of the foreseeability and causality requirements inherent in compensation for damage, the liability for damages would, as a rule, be limited to operations that the company has been able to influence.
	Burden of proof	• To ease the burden of proof of the injured party, the liability for damages could be combined with the option of reversing the burden of proof, in full or in part (in certain situations). • The rights to be protected should be weighed against the obligations imposed on the company.
	Conflict of laws	• The envisaged act could contain a conflict of laws provision to ensure that, despite the existence of international conflict of laws provisions, Finnish law would apply to claims for damages.
Sanctions	Administrative or criminal sanctions for non-compliance with the reporting obligation	• Any administrative sanctions could be linked to enterprises' reporting obligation.
	Administrative or criminal sanctions for non-compliance with the due diligence obligation	• Sanctions could be left out of the act, especially during the early stages. Any legislative sanctions should also be weighed against the end result that they are expected to achieve and that they can achieve.

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Judicial analysis on the Corporate Social Responsibility Act

Ernst & Young Oy has prepared a judicial analysis on the Corporate Social Responsibility Act commissioned by the Ministry of Economic Affairs and Employment. The analysis outlines the nature of the due diligence obligations that could be imposed on companies within a legislative framework in Finland. Due diligence refers to the process in which a company identifies, prevents and mitigates real and potential adverse impacts on human rights and the environment in its own activities, supply chain and other business relationships. The report explores possible regulatory options, their scope of application, supervision and sanctions under corporate social responsibility legislation. An analysis of corporate social responsibility regulation in the European Union and some other countries provides a backdrop for the report.

According to the analysis, business operations are already subject to various due diligence obligations, which require companies to assess and prevent risks associated with their operations. It would be possible to impose a duty of due diligence on companies regarding the environment and human rights within the framework of the national legal system. However, there are a number of issues to consider in relation to the legislation.

Online publications
ISSN 1797-3562
ISBN 978-952-327-553-9

Online version: julkaisut.valtioneuvosto.fi
Publication sales: vnjulkaisumyynti.fi