European Model Clauses, third draft

This draft is a consultation and not a final draft which still requires some polishing, amongst others regarding linguistic revision

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Introduction

1. General observations

Contracts are integral to corporate practice and to regulating global business operations, and increasingly address environmental and human rights issues in supply chains. Contracts can be a powerful tool to improve these practices, but their history is fraught. This project is an effort to improve contractual governance in order to better uphold human rights and environmental standards in global supply chains. The approach seeks to build on the strength and reach of contracts whilst moving away from contractual practices that have so frequently proven ineffective (if not counter-productive) in practice. The goal is to make human rights and environmental standards[1] a central part of contractual governance for both suppliers and buyers, as envisaged by the United Nations Guiding Principles on Business and Human Rights (UNGPs)[2] and the 2023 OECD Guidelines for Responsible Business Conduct.[3] Unanimously endorsed by the UN Human Rights Council in 2011, the UNGPs articulate companies' responsibility to respect human rights in order to satisfy that responsibility, their duty to carry out human rights due diligence (HRDD). HRDD should identify, prevent, mitigate and account for potential and actual adverse human rights impacts that may arise from their own activities or throughout their supply chains.

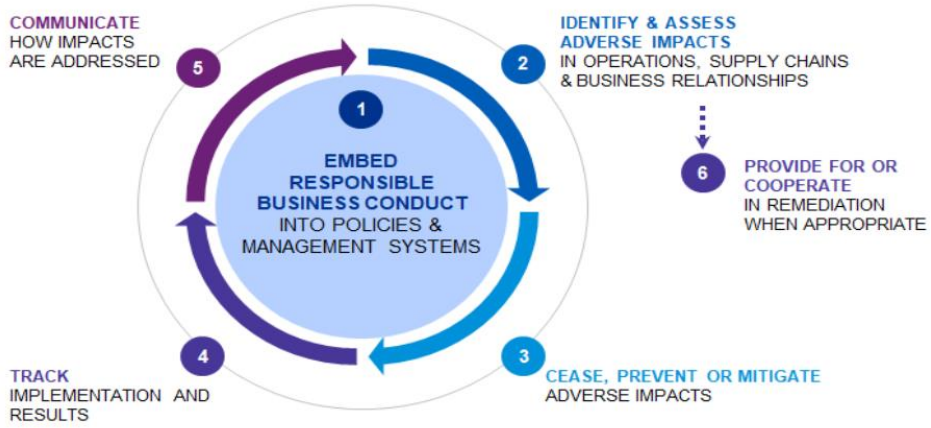
This type of due diligence, which focusses on the risks business operations pose for external stakeholders, is summarized in the following graphic from the OECD:[4]

[1] Such standards are generally stated in a corporate code. See for example Volkswagen, *Code of Conduct for Business Partners*, accessible at https://www.volkswagenag.com/presence/nachhaltigkeit/documents/policy-intern/2019_Code_of_Conduct_for_Business_Partners-DE-EN.pdf.

[2] https://www.ohchr.org/sites/default/files/documents/publications/guidingprinciplesbusinesshr_en.pdf.

[3] Accessible at http://mneguidelines.oecd.org/OECD-Due-Diligence-Guidance-for-Responsible-Business-Conduct.pdf.

[4] OECD Due Diligence Guidance for Responsible Business Conduct, p. 21,



Because risk identification, prevention, and mitigation required by HRDD extends beyond the business operations of the buyer itself and includes supply chains, buyers need to assure that their suppliers and sub-suppliers respect environmental and human rights standards. Because these commercial relationships are generally regulated by contracts, contractual mechanisms will play an important role, as reflected by current and proposed legislation.[5]

Although contract clauses and Supplier Codes of Conduct that seek to address environmental and human rights issues are frequent in practice, there has been little evidence that this has led to better environmental and human rights outcomes in supply chains. Frequent imbalances in bargaining power result in one-sided contractual clauses imposed by the most powerful party (generally the buyer) onto the weaker one (generally the supplier) which are not compatible with human rights or environmental standards.

These imbalances are exacerbated by the fact that many suppliers depend on a very limited number of buying companies,[6] and, particularly in less specialized sectors, buyers can easily switch suppliers. This dynamic can create a race to the bottom, with suppliers competing on ever lower pricing and timings at the cost of human rights or environmental standards.[7] Indeed, extreme pricing and timing pressure exerted by buyers can lead suppliers to be unable to pay a living or even minimum wage to their workers, and potentially spur them to have recourse to undeclared work, child labour and/or unpaid overtime.[8] In practice, many suppliers have reported taking orders at prices that would not even cover production costs.[9] In addition to production times often being too short, buyers have been reported to change or cancel orders at the last minute. Especially during the Covid-19 pandemic, many orders were cancelled by the buyers (even in cases of goods that had already been

[5] See Sect. 6 (4) No. 2 and 4 of the German Supply Chain Due Diligence Act (GSCCDA) and Artt. 7 (2b; 4) and 8 (3c; 5) of the European Commission`s Draft Corporate Sustainability Due Diligence Directive (CSDDD), available at https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52022PC0071 (hereinafter referred to as CSDDD).

[6] Daniel Vaughan-Whitehead & Luis Pinedo Caro, International Labour Office, Purchasing Practices And Working Conditions In Global Supply Chains: Global Survey Results, Inwork Issue Brief No. 10, 11 (2017), p. 6.

[7] Sarah Dadush, Contracting for Human Rights: Looking to Version 2.0 of the ABA Model Contract Clauses, 68 AM. U. L. REV. 1519 (2019).

[8] German government`s reasoning for the GSCDDA, BT-Drs. 19/28649, p. 43.

[9] Daniel Vaughan-Whitehead & Luis Pinedo Caro, International Labour Office, Purchasing Practices And Working Conditions In Global Supply Chains: Global Survey Results, Inwork Issue Brief No. 10, 11 (2017), p. 7.

manufactured and sometimes even already shipped), leaving suppliers unpaid and workers in the most precarious situations.

In addition, suppliers are generally expected to carry all the costs for compliance and verification which they often struggle to do, especially when they are SMEs with limited resources.[10]

Current contractual practices have not only failed to provide an effective mechanism to address these issues, but have even sometimes been an active part of the issues.

Similarly, the typical practice of using representations and warranties to assign all responsibility to suppliers in an effort to shift the risk of human rights and environmental violations is often doomed to failure. Guarantees of perfect performance are unrealistic in general, and the situation is exacerbated by differing codes and demands from different buyers. Such unrealistsic contractual mechanisms lead to turning a blind eye—or hiding—the problems and their causes, especially bease suppliers fear reprisal. Further, some companies do not monitor compliance with their codes, much less enforce them. Other companies use third-party audits, but these have often proved unhelpful as well. They sometimes are ill equipped to detect violations (e.g. interviewing workers in front of their employer), or are subject to audit fraud, or human rights issues such as forced labor may be difficult to detect. Other times the violations are so numerous that the auditors and the companies barely know how to catalogue and address the issues.

For example, some companies terminate contracts after a breach, which generally does not solve the environmental and human rights issue. On the contrary, it might worsen the problem since termination might force a supplier to contract other, more lenient buyers.

Contracts can be considerably more effective in delivering better human rights and environmental outcomes than they have been, and moving toward this outcome is the goal of this project. To be effective, contractual clauses need to be carefully crafted and provide for:

- responsibilities of both buyers and suppliers
- more uniform content, avoiding multiple and differing standards
- enforcement of the obligations so the environmental and human rights impact is remediated, with termination used only as a last resort
- access to information, including information gathered in grievance mechanisms
- dialogue and collaboration
- capacity building
- efficient and productive dispute resolution.[11]

[10] See Lidl`s case study "Spanish Berry HRIA", p. 18, accessed at: https://corporate.lidl.co.uk/sustainability/human-rights/hria/hria/spanish-berry, 11th of October 2022.

[11] Martijn Scheltema, The mismatch between human rights policies and contract law; improving contractual mechanisms to advance human rights compliance in supply chains, In: Accountability, international business operations, and the law (Liesbeth Enneking et.al. (eds.)), Routledge: London and New York 2020, para. 4, accessible at https://www.ohchr.org/Documents/Issues/Business/WGSubmissions/2018/MartijnScheltema.pdf.

2. Legislative developments in the EU

On February 23, 2022, the European Commission published a proposal for a Corporate Sustainability Due Diligence Directive (CSDDD),[12] seeking to turn the UNGPs due diligence expectations into hard law. An updated version of the proposed directive was adopted by the European Parliament on the 1st of June 2023.[13] In particular, the CSDDD aims to create a legally binding obligation for companies to carry out human rights and environmental due diligence (HREDD) throughout their own operations and those of their business partners across their value chains.[14]

The proposal introduces human rights and environmental due diligence obligations for large European and foreign companies meeting certain thresholds (defined in terms of number of employees and/or turnover). The obligations are accompanied by enforcement through national supervisory authorities and civil liability. Contractual provisions play a role throughout the proposal, and under Art. 12, the Commission is to adopt guidance – in consultation with Member States and relevant stakeholders - about voluntary model contract clauses to assist companies to meet the requirements of the Directive. It specifies that "those model contractual clauses shall stipulate, as a minimum the clear allocation of tasks between both contracting parties, in ongoing cooperation, and that contractual clauses shall not be such as to result in the transfer of responsibility for carrying out due diligence" (Art 12(1)(a) and that termination of such clauses should be avoided where contractual clauses are breached, and that instead, other appropriate measures to address the breach should be preferred to the extent as it is possible (Art 12(1)(b). The advantage of such model clauses also is that if they are applied by most buyers, suppliers face less diverging contractual requirements from their buyers. This may facilitate the implementation of human rights and environmental due diligence and lower cost for suppliers.[15]

The CSDDD recognizes that contracts have an important role to play - as a key component of the human rights and environmental due diligence exercise - to contribute to fostering respect for human rights, decent working conditions, and sustainable environmental standards within global supply chains.[16] Obviously, it has to be seen how the negotiations on the directive will evolve, but it seems

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[12] Available at https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52022PC0071 . For an overview of the obligations and the enforcement, contrasted with the German Supply Chain Due Diligence Act and the French Loi de Vigilance, see Brabant, Stephane, Bright, Claire, Neitzel, Noah; Schönfelder, Daniel: *Due Diligence Around the World: The Draft Directive on Corporate Sustainability Due Diligence (Part 1), VerfBlog,* 2022/3/15, https://verfassungsblog.de/due-diligence-around-the-world/ and Brabant, Stephane, Bright, Claire, Neitzel, Noah; Schönfelder, Daniel: *Enforcing Due Diligence Obligations: The Draft Directive on Corporate Sustainability Due Diligence (Part 2), VerfBlog,* 2022/3/16, https://verfassungsblog.de/enforcing-due-diligence-obligations/

[13] Available at https://www.europarl.europa.eu/doceo/document/TA-9-2023-0209_EN.pdf.

[14] More regulation is either in force or envisaged which will require of facilitate the implementation of corporate sustainability due diligence, such as the Corporate Sustainability Reporting Directive (EU 2022/2464), accessible at https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32022L2464), the envisaged Forced Labour Regulation (Com (2022) 453 Final, accessible at https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52022PC0453), the proposal for a deforestation regulation Com(2021) 716 final, accessible at https://eur-lex.europa.eu/resource.html?uri=cellar:b42e6f40-4878-11ec-91ac-01aa75ed71a1.0001.02/DOC_1&format=PDF and (Articles 47-53 of the) Battery Regulation EU 2023/1542, accessible at https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32023R1542.

[15] Cf. the commentary to the OECD Guidelines to II (General Policies), para. 26.

[16] See also the commentary to the OECD Guidelines to II (General Policies), para. 23.

quite sure contractual approaches will remain part of the due diligence process as envisaged by the CSDDD.

A central goal of the EMC project is to move away from contracts that are ineffective and perhaps even counterproductive and to provide clauses that will integrate with HREDD standards, implement them, and support the goals of the CSDDD and similar legislation.

The CSDDD itself contemplates the use of contracts is part of humanrights and environmental due diligence: companies can use well-designed contractual provisions as a means to assist in preventing potential adverse impacts (Art 7 (2)(b)), as well as bringing adverse impacts to an end (Art 8 (3)(c)). For both, the proposal states that companies should use contractual provisions with business partners to give weight to a company's code of conduct and help ensure compliance, and that such provisions shall be "fair, reasonable and non-discriminatory" (Art 7(4)(2) and Art 8(5)(2)). Both provisions require buyers to assess whether the business partners "can reasonably be expected to comply with those provisions" (Art 7(4)(2) and Art 8(5)(2)(b).

They also envisage the possibility of requiring business relationships to establish corresponding reasonable, non-discriminatory and fair contractual provisions with their partners that are part of the value chain. Both provisions clarify that such contractual provisions shall be accompanied by measures to support carrying out due diligence (Art 7(4)(1) and Art 8(5)(1).

Importantly, the European Parliament proposal clarifies that contractual provisions shall not result in the transfer of responsibility for carrying out due diligence to business relationships in the supply chain (Art 7(4)(2) and Art 8(5)(2).

Although the proposal applies to only certain large companies, it envisions that human rights and environmental due diligence obligations will flow through to SMEs through contractual measures and include special provisions in their respect and notably the fact that, where measures to verify compliance are carried out in relation to SMEs, the cost of independent third-party verification shall be borne (fully or in part) by the buyer.

Though this might not address all the potentially problematic behavior covered by Schedule Q in the Model Contract Clauses for Supply Chains (MCCs), see below paragraph 3, it does recognize that often, due to an imbalance between the parties, all responsibility and cost for complying with codes of conduct fall on the smaller companies, while the causes of the violations can equally lie with the larger companies.

Responsible purchasing practices, which means the behavior of the buyer in the contractual relationship, are explicitly mentioned in the European Parliament's version of the CSDDD, which notably requires companies to "adapt business models and strategies, including purchasing practices, including those which contribute to living wages and incomes for their suppliers", in order to prevent potential adverse impacts or to bring to an end or mitigate actual adverse impacts (Art 7(2)(c)(a) and Art 8(3)(d)(a) and to "develop and use purchase policies that do not encourage actual adverse impacts on human rights or the environment".

The proposal clearly provides for the possibility to temporarily suspending commercial relations or terminating the business relationships where the potential adverse impacts could not be prevented or adequately mitigated or where the actual adverse impacts could not be brought to an end or mitigated and where there is no reasonable prospect of change (Art 7(5)(1) and Art 8(6)(1) but

requires the company to assess whether the adverse impacts of doing so would be greater than the adverse impact which is intended to be prevented or mitigated and to take steps to ensure a responsible exit (Art 7(5)(1) and Art 8(6)(1)(a)).

Beyond the legislative developments in the EU different member states have also implemented legislation on corporate sustainability due diligence. For example, France, Germany and the Netherlands have adopted legislation on this topic. The German law explicitly refers to contractual mechanisms like the draft directive as proposed by the European Commission.[17] Other European countries outside the European Union, like Norway, have also adopted legislation.

3. The ABA Model Clauses for Supply Chains

In an attempt to address some of the issues identified in paragraph 1, a working group of the American Bar Association Business Law Section developed Model Contract Clauses to Protect Workers in Supply Chains.[18] These model contract clauses (MCCs) are a major shift in contract design, reflecting both recent research and thinking about what organizational strategies are most effective, and recent and ongoing legislative developments, including not only US legislation but also anticipating the likely mandatory human rights due diligence law in the European Union.[19] Instead of a typical regime of representations and warranties, with concomitant strict contractual liability, these clauses provide for a regime of human rights due diligence, requiring the parties to take appropriate steps to identify and address adverse human rights impacts. As a result, suppliers are less incentivized to hide problems for fear of contractual sanctions: they do not have to pretend that no human rights problems exist, but they have to show that they are implementing measures to address them.

The most prominent shift in the MCCs is that buyers share contractual responsibility for human rights with their suppliers and sub-suppliers. The MCCs include principles of responsible sourcing to avoid contributing to human rights violations, for example, negotiating prices that allow the supplier to pay adequate wages, see Art. 1.3.[20] If a human rights violation occurs, remediation costs are divided between buyer and supplier, depending on who caused it, Art. 2.3 e.[21] Merely changing purchasing without contractually giving the supplier enforcement rights lacks effectiveness as the supplier would be reluctant to address human rights problems. Concrete obligations of buying

[17] An English version is accessible at https://www.bmas.de/SharedDocs/Downloads/DE/Internationales/act-corporate-due-diligence-obligations-supply-chains.pdf?__blob=publicationFile&v=3.
[18] These clauses may be accessed at https://www.americanbar.org/content/dam/aba/administrative/human_rights/contractual-clauses-project/mccs-full-report.pdf.
[19] See the abstract of this project (note 4), p. 1 and 2.
[20] Principled Purchasing Project, American Bar Association: *Model Contract Clauses to Protect Workers in International Supply Chains, Version 2.0* Art. 1.3 https://www.americanbar.org/content/dam/aba/administrative/human_rights/contractual-clauses-project/mccs-full-report.pdf parties to the agreement may also agree on the responsible sourcing practices included in Schedule Q: *Responsible Purchasing Code of Conduct: Schedule Q Version 1.0* https://www.americanbar.org/content/dam/aba/administrative/human_rights/contractual-clauses-project/scheduleq.pdf
[21] Principled Purchasing Project, American Bar Association: *Responsible Purchasing Code of Conduct: Schedule Q Version 1.0* https://www.americanbar.org/content/dam/aba/administrative/human_rights/contractual-clauses-project/scheduleq.pdf

companies in the contract give suppliers some leverage and assurance to proactively and collaboratively address problems.

To address human rights issues throughout the entire supply chain, the MCCs include an obligation on the Supplier to ensure that their Suppliers and sub-suppliers in turn implement human rights due diligence requirements, Article 1.2. The ABA MCCs also stress the importance of providing remedy to those harmed in case of a breach, rather than merely using typical contractual remedies such as money damages which only benefit the contracting parties. In constructing remediation plans, suppliers need to consult with the affected stakeholders. Before terminating a contract, buyers need to "consider the potential adverse human rights impacts and employ commercially reasonable efforts to avoid or mitigate them".[22]

4. European Working Group

4.1. Introduction

The European Working Group (European WG) is an independent working group which was formed in 2021 and is composed of legal practitioners and academics representing France, Germany, Italy, the Netherlands, Poland, Portugal and Spain, along with experts in the law of the EU, the US and UK. Building on the MCCs,[23] it seeks to develop European Model Clauses (EMCs) adapted to the European context and aligned with the CSDDD, UNGPs, the 2023 OECD Guidelines for Responsible Business Conduct, and related guidance.

Identifying strategies and templates for more effective, Human Rights and Environmental Due Diligence (or corporate sustainability due diligence as referred to in the CSDDD)-aligned contracting is the goal of the European WG. Contracts are vehicles for implementing businesses' human rights and environmental policies across borders and throughout the supply chain, and the European Model Clauses for Supply Chain Contracts (EMCs) seek to harness this contractual power. In practice, studies have shown that contracts are one of the most commonly used tools by companies to carry out Human Rights and Environmental Due Diligence.[24]

However, it is important to acknowledge from the outset that supply chain contracts are not - and should not be - the only means for companies to carry out human rights and environmental due diligence. Rather, contractual clauses should be seen as one tool in the toolbox available to companies in carrying out due diligence. As such, contractual clauses should be implemented as part of broader corporate sustainability due diligence.[25] Appropriate contractual clauses can help achieve the goals of the CSDDD and similar legislation, and certainly contracts cannot be ignored. In the past,

[22] ABA (note 15) p. 22.

[23] See for these clauses https://www.americanbar.org/content/dam/aba/administrative/human_rights/contractual-clauses-project/mccs-full-report.pdf.

[24] L. Smit, C. Bright, R. McCorquodale, et al. 'Study on Due Diligence Requirements through the Supply Chain', Study for the European Commission, February 2020, p. 152, accessible at: https://op.europa.eu/en/publication-detail/-/publication/8ba0a8fd-4c83-11ea-b8b7-01aa75ed71a1/language-en.

[25] See also the new paragraph 1a to Article 12 proposed by the European Parliament, European Parliament, Committee on Legal Affairs, Draft Report on the proposal for a directive of the European Parliament and of the Council on Corporate Sustainability Due Diligence and amending Directive (EU) 2019/1937, 2022/0051(COD), p. 98, accessible at https://europa.pvda.nl/wp-content/uploads/sites/458/2022/11/due_diligence_report.pdf.

contractual clauses have often not been crafted in a way that is compatible with human rights and/or environmental standards, and the EMCs seek to address this issue. The use of model contract clauses which are aligned with the CSDDD, UN Guiding Principles and 2023 OECD Guidelines for Responsible Business Conduct will make achieving the objectives of the CSDDD more operationally likely.

As the CSDDD aims to create a legal obligation to undertake human rights and environmental due diligence and to implement grievance mechanisms, as well as retrieving aggregated information from these mechanisms, the only fashion this legal obligation can be transposed into supply chains is through contracts. Contracts are also indispensable for information sharing and documentation for the use of businesses (including management and owners) on the environmental and human rights situation in supply chains, as no obligation would exist for suppliers that are not in scope of the CSDDD and in places beyond the effective jurisdiction of public (supervisory) authorities to provide this information otherwise. This may be relevant for regulators, public supervisory authorities, and courts. Contracts are especially useful for generating human rights and environmental information from within the supply chain given that suppliers that are not in scope of the CSDDD may not be bound to provide this information otherwise. Access to this information may also assist buyers to meet obligations under European reporting requirements. Beyond this, model contracts can be reviewed and revised more easily and more quickly than regulation or public policy. This enables more frequent and continuous improvement in light of learning, experience and changing circumstances.

Furthermore, European model contract clauses can help generate a European level playing field and reduce costs for businesses. If the model clauses become an often-applied model, this will enhance fair competition and will incentivize companies to implement comparable human rights and environmental practices aligned with the CSDDD. Widely adopted model clauses can reduce cost for businesses as they do not need to reinvent the wheel by drafting their own contractual provisions, at considerable cost, especially if they have to engage external counsel (as may frequently be necessary for smaller and medium sized entities). {Does this raise competition issues? Someone who knows about European competition law should consider this.}

4.2. Content of the EMCs

The EMCs seek to improve the current contracting practices that have proven so clearly insufficient. In particular, they seek to implement more balanced approaches in supply chains, with clauses that encourage cooperation, information sharing and fair dealings, including through responsible purchasing practices. They seek a balance between buyers and suppliers, as well as worker-focused provisions on internal grievance mechanisms, human rights remediation, and options for third-party rights and responsible exit. Thus the EMCs, like the MCCs, move away from the unilateral model where only one party bears responsibility for ensuring that human rights and environmental standards are upheld, towards a model of shared responsibility where both parties are obligated to carry out HREDD and to cooperate and support one another in doing so. The EMCs are able to take the shared responsibility principle further thanks to the legislative backdrop against which the European WG is operating.

Specifically, the clauses shift away from a regime of static, supplier-only, representations and warranties that require the supplier to guarantee that there are no and never will be any human rights issues in its supply chain towards a regime of human rights and environmental due diligence, under which both parties are responsible for upholding human rights and environmental standards.

Three key shifts deserve highlighting:

1. **Human Rights and Environmental Due Diligence:** buyer and supplier must *both* conduct human rights and environmental due diligence before and during the term of the contract.
2. **Buyer Responsibilities:** to discharge their respective HREDD obligations and avoid causing or contributing to adverse impacts, *both* buyer and supplier must engage in responsible sourcing and purchasing practices.
3. **Remediation-first:** in the event of an adverse impact, stakeholder-centred human rights remediation should come before or in conjunction with conventional contract remedies, such as termination, rejection, and money damages. Moreover, if the buyer contributed to the adverse impact (e.g., through its purchasing practices), then the buyer must participate in providing remediation to victims.

The EMCs also provide for reasonable assistance and support by buyers for suppliers who need help complying with the goals of the CSDDD.

The EMCs seek to adapt these new contracting strategies to the European context, in alignment with the CSDDD. The European WG is adapting and expanding the ABA MCCs to be compliant with European public law (such as EU directives and regulations), private law (the civil law system and especially contract law in member states with an eye to the Draft Common Frame of Reference), and with the European drafting style (concise rather than comprehensive).

This approach is aligned with the amendment proposed by the European Parliament to recital 39 of the CSDDD, which reads:[26]

> 'The simple inclusion of certain contractual provisions in company contracts should not be considered sufficient to satisfy that company's legal obligations to carry out due diligence under this Directive, nor should contractual provisions transfer responsibility to any party for carrying out due diligence. Moreover, contractual provisions should be fair and reasonable under the circumstances and reflect the joint responsibility of parties to conduct due diligence in ongoing cooperation, with an emphasis on taking appropriate measures to bring adverse impacts to an end, rather than termination or suspension in the case of infringements or breaches which may have given rise to actual adverse impacts. Companies should also assess whether the business partner can reasonably be expected to carry out due diligence as provided for in this Directive, taking account of, amongst other factors, the sector, context and level of risk of the business relationship and the business partner; the resources, experience, history and credentials of each business partner; and any support given by the company to its business partner. Often contractual terms are unilaterally imposed on a supplier by a buyer, and any breach thereof is likely to result in unilateral action by the buyer such as termination or disengagement. Such unilateral action is not

[26] See 2022/0051(COD), p. 29.

appropriate in the context of due diligence and would probably itself result in adverse impacts.'

Corporate sustainability due diligence as envisaged by the EMCs involves realistic identification and mitigation of risks rather than unrealistic or uninformed allocation of risk to suppliers through representations, warranties, or assurances that promise perfect compliance. The EMCs focus on practical problem identification and dispute resolution rather than arbitration or litigation. They emphasize that remediation is a better strategy than termination.[27] The EMCs suggest best practices for responsible exit if termination is necessary as a last resort. The EMCs also acknowledge the need to engage with and meaningfully consult stakeholders and rights-holders as well as buyers and suppliers and recognize all of them as relevant participants in connection with supply chain contracts.[28]

Finally, the EMCs aim to be modular and scalable to take into account different capabilities of large corporates versus SMEs.

The format of the EMCs will depart significantly from the MCCs in that each provision will include: (1) the model clause itself, (2) a general commentary explaining the objective of the clause (possibly including the guidance on responsible purchasing set out in the MCCs' Schedule Q, also referred to as the Buyer Code), (3) a commentary explaining best practices and referring to documents that may assist in implementing the clause, and (4) where relevant, guidance on implementing the clause in different member states with an eye to the Draft Common Frame of Reference.

The EMCs are intended to serve as an example of contractual clauses that can be implemented in (existing) supply chain contracts. If so, it will be important to ensure that the implemented provisions dovetail with the main sales agreement, including in relation to i) remedies, ii) termination iii) disclaimers, and iv) dispute resolution and confidentiality. They will need to be adapted to avoid duplication or uncertainty when combined with the provisions in the main sales agreement.

The users will need to decide whether the model is used and to what extent the EMCs are adopted in the supply chain contracts. However, departures from the EMCs, and adherence to more traditional contractual language, increases the risk that these supply chain contracts will be incompatible with due diligence as required by the CSDDD.

The model is general and has only very limited specific guidance for various sectors in which supply chain contracts are deployed. That said, the approach suggested in the EMCs is generally applicable across sectors and can be adapted without unreasonable effort for specific sectors.

[27] The European Parliament in its proposed addition to recital 41 also emphasize that a company the assess the adverse impacts of a termination decision in line with its due diligence obligations. See 2022/0052(COD), p. 31. See also the amendment to Articles 7(5)(2), 8(6)(2) and 12(1b), 2022/0052(COD), p. 74, 85, 97 and 98.
[28] See also the new recital 44 a proposed by the European Parliament and the new subparagraph (da) proposed to Article 7(2), 2022/0052(COD), p. 35, 36, 70 and 71.

4.3 Further development of the EMCs

The first draft of the European Model Clauses was discussed within the working group in Lisbon on 12 and 13 September 2022. The next step was to implement the revisions suggested during this meeting, which has resulted in this second draft (April 2023). This draft was discussed by the working group at a meeting held in Rotterdam on 15 and 16 May 2023 and has lead to a third draft that will be shared for a limited consultation in October/November 2023. The input received during this limited consultation will be implemented in a draft ready for broader consultation. The European WG plans to organize, preferably in collaboration with others, a public consultation as well as consultations directed at specific stakeholders such as businesses (or their trade associations and organizations), civil society organizations, representatives from affected stakeholders, regulators and public supervisors during the summer of 2024. After implementing the results of the consultations, a final version will be circulated, revised, and published. After publication the working group plans to regularly update the EMCs, building on improved practices, continued consultations and conversations with relevant stakeholders, and changing global supply chains. It may contemplate to provide sector specific models and/or guidance as well.

5. Members of the working group

The European working group currently consists of the following members (alphabetically by country)

Maria Pia Sacco (EU Law)

Salli Swartz (EU law)

Stéphane Brabant (France)

Sarah Dadush (France)

Gilles Lhuilier (France)

Anna Beckers (Germany)

Bettina Braun (Germany)

Michael Riegner (Germany)

Daniel Schönfelder (Germany)

Michaela Streibelt (Germany)

Angelica Bonfanti (Italy)

Achille Caliò Marincola Sculco (Italy)

Roberto Randazzo (Italy)

Martijn Scheltema, Co-chair (Netherlands/EU law)

Stanislaw Drozd (Poland)

Beata Faracik (Poland)

Claire Bright (Portugal/Spain)

Maria Folque (Portugal/Spain)

Carmen Marquez Carrasco (Portugal/Spain)

Jose Maria de Paz (Spain)

Noemi Marques de Magallanes (Spain)

Jaime de Blas (Spain)

Jordi Gras (Spain)

Encarna Cordero (Spain)

Andrea Sanchez (Spain)

Mariona Bernaus (Spain)

Rita Prates (Portugal/Spain)

Rachel Barrett (UK)

David Snyder, Co-chair (US)

6. The European model clauses to undertake Corporate Sustainability Due Diligence in Supply Chains

Unlike the MCCs, the following European model clauses to undertake Corporate Sustainability Due Diligence in Supply Chains are embedded in the European regulatory landscape in which contractual mechanisms in supply chains play a role. They are a means through which Corporate Sustainability Due Diligence can be undertaken in supply chains, obviously in addition to other means of undertaking such due diligence.

The EMCs, although built on the ABA MCCs, implement an adapted approach compared to its US predecessor (which is currently being reviewed), not only because of the (current and future) legislative requirements in the EU and its member states, but also to provide insight in necessary adaptations which may be required in specific legal (contract law) systems of the EU member states as well as more practical guidance in connection with the model clauses.

Therefore, the following model clauses are elaborated as follows. First the text of the model clause is elaborated per Article. After this a general commentary is provided with the background of the Article and its objectives as well as other observations which may be helpful or should be borne in mind when implementing this Article in a supply chain contract. The general commentary is followed by best practices, where available, in order to provide more practical guidance regarding the implementation of the Article. Finally, country specific observations are added where the contract law of EU member states requires deviation from the general model or where such deviation would

be recommendable from the point of view of national contract law of this member state. Obviously, other specific legislation should be considered as well, such as the GDPR or competition law. This is not all explicitly referred to in this model as that would make it unwieldy and would render it quite challenging to negotiate or implement.

Finally, the model clauses refer to Schedule Q which is an annex to the MCCs, with responsible sourcing practices for buyers, as the current purchasing practices often contribute to adverse impacts, as explained above.

The European Model Clauses

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Definitions

Adverse Impact: Adverse Environmental Impact and/or Adverse Human Rights Impact which one or both parties have either caused, contributed to, or are directly linked to their products, services, and business relationships.

Adverse Environmental Impact: means an adverse impact on the environment [which brings about an Adverse Human Rights Impact][resulting from the violation of one of the prohibitions and obligations pursuant to the international environmental conventions listed in the Annex, Part II of the EU Corporate Sustainability Due Diligence Directive][resulting from the violation of one of the prohibitions and obligations pursuant to Schedule P].

Adverse Human Rights Impact: means an adverse impact on protected persons resulting from the violation of one of the rights or prohibitions listed in the Annex, Part I Section 1, as enshrined in the international conventions listed in the Annex, Part I Section 2 of the EU Corporate Sustainability Due Diligence Directive][Schedule P].

Agreement: this agreement.

Buyer: Party [X] to this Agreement.

CSRD: Corporate Sustainability Reporting Directive, Directive (EU) 2022/2464 of 14 December 2022 amending Regulation (EU) no. 537/2014, Directive 2004/109/EC, Directive 2006/43/EC and Directive 2013/34/EU, Official Journal of the European Union of 16 December 2022, L 322/15.

Effective Date: the date on which obligations implemented in this Agreement become effective.

Human Rights and Environmental Due Diligence: a process appropriate to the size and circumstances of the party implementing it to identify, prevent, mitigate, cease, minimize, track and communicate Adverse Impact.

ESRS: European Sustainability Reporting Standards, Commission Delegated Regulation supplementing Directive 2013/34/EU and annexes 1 and 2.

Goods: the products or materials provided by Supplier as listed in Annex [x] to this Agreement.

Living Wage: the higher of the minimum wage (if applicable), or wages required for the basic needs of workers and their families as determined using a reputable benchmark to be agreed between the parties.

Representatives: [officers, directors, employees,] agents and all subcontractors, consultants and any other person providing staffing for Goods or services to Buyer required by this Agreement.

[Schedule P: a list attached to this Agreement with international environmental and human rights conventions non-compliance with which may cause environmental degradation or pollution and/or human rights abuse].

[Schedule Q: a list attached to this Agreement setting forth the responsible purchasing practices the Buyer shall make a best effort attempt to implement.][29]

Severe Adverse Impact: an Adverse Impact which is large scale, has a big impact by its nature or is irreversible.

SME: means a micro, small or a medium-sized enterprise, irrespective of its legal form, that is not part of a large group, as those terms are defined in Article 3(1), (2), (3) and (7) of Directive 2013/34/EU.

Supplier: Party [Y] to this Agreement.

[29] An example of such a list can be found in Schedule Q of the ABA Model Clauses accessible at https://www.americanbar.org/content/dam/aba/administrative/human_rights/contractual-clauses-project/scheduleq.pdf.

Article 1 Mutual Obligations with Respect to Due Diligence in Supply Chains

As of the Effective Date of this Agreement, Buyer and Supplier each agree:

1.1 Environmental and Human Rights Due Diligence

(a) Buyer and Supplier each covenants to cooperate with each other to establish and maintain a Human Rights and Environmental Due Diligence process in connection with the Goods and services governed by this Agreement appropriate to its size and circumstances to identify, prevent, mitigate, cease, minimize, track and communicate how each of Buyer and Supplier addresses the potential and actual Adverse Impacts of its activities directly or through their supply chains. In case the Supplier is an SME, he is only required to participate in environmental and human rights due diligence measures of the Buyer. Such human rights and environmental due diligence shall be consistent with the 2011 United Nations Guiding Principles on Business and Human Rights and with guidance from the Organisation for Economic Cooperation and Development for the applicable party's sector [or, if no such sector-specific guidance exists: shall be consistent with the 2018 OECD Due Diligence Guidance for Responsible Business Conduct (the OECD Due Diligence Guidance)]. Such due diligence shall not prejudice due diligence requirements included in specific European and member state legislation.

(b) In establishing and maintaining the Human Rights and Environmental Due Diligence process set out in Clause 1.1, Buyer and Supplier must, meaningfully engage stakeholders such as workers, local communities, as well as other individuals or groups potentially or actually affected by an Adverse Impact, including by violations of Schedule Q ("Stakeholders"). Such stakeholder engagement must be on-going, responsive, and effective. They may prioritize engagement according to severity and likeliness of adverse impacts.

(i) To identify their Adverse Impacts accurately, Buyer and Supplier shall seek to understand the concerns of Stakeholders by consulting them directly in a manner that takes into account language and other potential barriers to effective engagement. Where such consultation is not possible, the parties shall consider reasonable alternatives such as consulting credible, independent expert resources, including human rights defenders and others from civil society.

(ii) As part of the consultation process, Buyer and Supplier shall take steps to provide Stakeholders with pertinent information regarding their human rights and environmental position, Schedule Q, and other relevant information necessary for Stakeholders to meaningfully engage in the parties' Human Rights and Environmental Due Diligence process.

(iii) Where Stakeholders reasonably request additional information from Buyer and Supplier, each party shall, within a reasonable time frame, either provide such information or submit a written justification for not doing so.
The parties shall determine which Stakeholders to engage and the intensity of the engagement based on the degree of the Adverse Impact on such Stakeholders.

Buyer and Supplier shall adequately document the Stakeholder consultation process to enable Buyer to comply with the relevant reporting requirements under applicable law.

(c) [Buyer and Supplier each] [Supplier] shall cause each of its employees and shall make best efforts to cause other Representatives to disclose on a [yearly or other timeframe] basis both forward looking and retrospective for a period of [six] months, as well as qualitative and quantitative information, regarding due diligence measures implemented by the Supplier and disclosure of actual or potential severe Adverse Impacts on the Supplier level when they occur or the Supplier becomes aware of a potential Severe Adverse Impact. The foregoing obligation does not apply if [the party which shall provide information][Supplier] is governed by sustainability reporting obligations under domestic law implementing the CSRD and has published such a report.

As far as allowed under the applicable laws, each party may request the other to provide additional due diligence-related information, so long as such requests are reasonable and necessary for the requesting party to effectively carry out its own due diligence obligations under this Agreement and applicable law.

All of the information provided in relation to this Agreement shall be accurate, provided in a digital format, and enabling the receiving party to comply with the CSRD and the ESRS [and any other applicable reporting obligations], to conduct risk analyses and to adapt the due diligence process if required. [Buyer has the right to annually and ad hoc request information in relation to potential and actual adverse impacts by way of a questionnaire. The questionnaire must be based on the Buyer's findings from their risk analysis. Such questionnaires shall be reasonable in scope and, whenever possible, designed to reduce the administrative burden for the responding party and to be consistent with the questionnaires developed by relevant industry associations or used by other companies operating in the same industry and in the same capacity as [Buyer] [Buyer and Supplier, respectively], Article 1.3 (i) applies.

(d) For the avoidance of doubt, each party is independently responsible for upholding its obligations under this Section 1.1, and a breach by one party of its obligations under this Section 1.1 shall not relieve the other party of its obligations under this Agreement.

(e) Environmental and Human Rights Due Diligence hereunder shall include implementation and monitoring of a risk-assessment, prevention and, if applicable, remediation plan commensurate with Article 2.3 to address issues identified by due diligence that was conducted before the Effective Date.

1.2 Compliance Throughout the Supply Chain

Supplier shall make a best effort to ensure that each of its Representatives acting to provide Buyer with Goods and/or services in connection with this Agreement shall engage with its own Suppliers and any other Representative in due diligence in accordance with Section 1.1. [Supplier shall make a best effort to ensure that its own suppliers and any other Representative implement the [same][comparable][at least as protective] obligation on their suppliers and/or any other representatives. Such relationships shall be formalized in written contracts.] [Any subcontracting (including hiring of subsuppliers or the like) after the effective date is permitted only after Supplier has conducted Human Rights and Environmental Due Diligencerisk analysis on such subcontractor, and such subcontractor has agreed to the Human Rights and Environmental Due Diligence responsibilities stated herein. [All subcontracting [where the total contract price for such

subcontract or in aggregate with related subcontracts is greater than above Euro[___]] must be approved in advance in writing by Buyer. Such approval is not to be unreasonably withheld, delayed, or conditioned, provided that Buyer may withhold such approval if it reasonably determines that such subcontracting would, individually or in aggregate with related subcontracts, materially increase the risk of Adverse Impacts][Supplier shall promptly inform Buyer of all subcontracting [where the total contract price for such subcontract or in aggregate with related subcontracts, is greater than Euro[___]].

Supplier shall keep records of such written contracts to demonstrate compliance with its obligations under this Agreement. Supplier shall deliver such records as well as relevant information regarding an Adverse Impact to Buyer to the extent Supplier avails over such information and as far as allowed by law if Buyer has substantiated reasons to believe a human rights or environmental issue has emerged or is informed of such issue in the value chain the Supplier is part of and where relevant to Buyer's due diligence as far as legally allowed.

1.3 Buyer's Commitment to Support Supplier Compliance

(a) Commitment to Responsible Purchasing Practices

Buyer commits to support Supplier's implementation of Human Rights and Environmental Due Diligence by engaging in responsible purchasing practices [in accordance with Schedule Q] and only imposing fair, reasonable and non-discriminatory obligations on SMEs.

(b) Reasonable Assistance

If Buyer's risk analysis determines Supplier requires assistance to implement Human Rights and Environmental Due Diligence, or after a reasonable and substantiated request from the Supplier for this assistance, Buyer shall employ commercially reasonable efforts to provide such assistance[, which may include Supplier training, upgrading facilities, advice on measures to verify compliance [and] strengthening management systems [[, and financing, for example, through direct financing, low-interest loans, guarantees of continued sourcing, and assistance in securing financing][30]] to the extent legally permitted. Buyer's assistance shall not be deemed a waiver by Buyer of any of its rights, claims or defenses under this Agreement or under applicable law. Supplier shall collaborate with Buyer and provide reasonable assistance to Buyer to the extent required to implement the due diligence process as referred to in Section 1.1.

(c) [Pricing

(i) Buyer and Supplier shall collaborate to agree on a price [, taking into account the size of the contract ,] that accommodates the costs associated with implementing and upholding Human Rights and Environmental Due Diligence, including payment of the applicable minimum wage or a Living Wage, whichever is higher, that is appropriate to the region, sector, and skill level. If the payment of a Living Wage is not immediately feasible, then Buyer and Supplier shall commit to a progressive, evolving pricing schedule to pay a living wage within a reasonable time. Supplier shall ensure that the funds being paid by Buyer to ensure the payment of the Living Wage are used solely for that purpose. Supplier shall document that such funds are being used as agreed, and in the absence of satisfactory documentation, such funds shall be reimbursed to Buyer. If necessary, Buyer may set off

[30] The CSDDD especially mentions this for SME Suppliers.

any unreturned funds against any amount that Buyer owes Supplier. [Where possible, Buyer and Supplier shall cooperate to utilise open book costing approaches to determining price.]

(ii) If there is a material increase in input costs that increases the risks of any Adverse Impacts [and Supplier is an SME], Buyer and Supplier shall collaborate to agree on alternative terms to mitigate and prevent such Adverse Impacts. Such alternative terms may include price adjustments, advance payments, credit facilities, schedule changes, or extended contract terms. Buyer may require Supplier to provide documentation of the increase in input costs. In the event of a price adjustment, Supplier shall document that the funds are being used as agreed, and in the absence of satisfactory documentation, such funds shall be returned to the Buyer. If necessary, Buyer may set off any unreturned funds against any amount that Buyer owes Supplier.

(d) Commercial Terms (Payment and Delivery)

Buyer shall collaborate with Supplier to agree on commercial terms, including payment and delivery terms, that will support Buyer and Supplier's performance of their obligations under this contract, prevent and mitigate Adverse Impacts and which commercial terms are in alignment with Schedule Q. The terms will clearly indicate the time and place for (a) the transfer of ownership; (b) the transfer of risk of loss; (c) the Buyer's obligation to accept the Goods; and (d) the Buyer's obligation to pay.

(e) Commercial Compliance

Whereas the parties understand that noncompliance with commercial terms can result in Adverse Impacts, the parties shall abide by the terms of this contract, including with respect to terms on price, payment, delivery, or orders. To further ensure that commercial conduct does not result in Adverse Impacts, and in keeping with the obligation of good faith, Buyer shall not vary the terms of this contract unilaterally, nor shall Buyer impose additional costs or employ other commercial devices to obtain unnegotiated benefits.

(f) Order Changes

For any material change of an order (including, but not limited to, change orders, quantity increases or decreases, or changes to design specifications) requested by Buyer or Supplier, Buyer and Supplier shall consider the potential environmental and human rights impacts of such change and take action to avoid or mitigate any Adverse Impacts, including by amending the change [consistent with Schedule Q]. If Buyer and Supplier fail to agree upon modifications and/or amendments that would avoid an Adverse Impact, then either party may [insist on performance as agreed upon in this Agreement][initiate dispute resolution in accordance with Article 7].

(g) Excused Non-Performance

If (i) Supplier provides notice and reasonably satisfactory evidence to Buyer that an Adverse Impact is reasonably likely to occur because of a requested modification or because of a reasonably unforeseeable, industry-wide or geographically specific, material change to a condition affecting Supplier; (ii) the parties cannot agree on a solution that avoids this Adverse Impact (which may include subcontracting); and (iii) Supplier elects not to perform in order to avoid this Adverse

Impact, then the parties hereby agree that this Agreement or a specific purchase order hereunder may be terminated in whole or in part by Supplier and that Supplier shall not be in default of its obligations under this Agreement as a result of such non-performance.

(h) Responsible Exit

In any termination of this Agreement,[31] whether due to a failure by a party to comply with this Agreement or for any other reason (including the occurrence of a force majeure event or any other event that lies beyond the control of the parties), the terminating party shall (i) consider the potential Adverse Impacts [, including meaningful consultation of (representatives of) impacted stakeholders,] and employ achievable, proportionate and reasonable efforts to avoid or mitigate them; and (ii) provide reasonable notice to the other party of its intent to terminate this Agreement, unless the non-compliance with this Agreement by the other party is intentional and/or section 2.5 applies. Termination of this Agreement shall be without prejudice to any rights or obligations accrued prior to the date of termination, including, without limitation, payment that is due for acceptable Goods produced by Supplier pursuant to Buyer's purchase orders before termination.

(i) Recognition

Where Buyer seeks to employ due diligence measures such as, but not limited to, questionnaires, audits, and scorecards in its Human Rights and Environmental Due Diligence processes, Supplier may to the extent allowed by law provide Buyer with a recent equivalent document, and Buyer shall accept such equivalent document [or a portion of the equivalent document to the extent that it meets the Buyer's minimum standards], unless it reasonably considers that such equivalent document [entirely] fails to satisfy Buyer's minimum standards. A recent CSRD report is recognized as a recent equivalent document. At the request of Supplier, Buyer shall, to the extent permissible under competition laws, coordinate with Supplier and other buyers to minimise inconsistencies between various due diligence measures employed.

(j) Positive incentives for compliance

Buyer and Supplier shall collaborate to establish benchmarks to assess sustainability performance. If possible, given the state of business commitments and market demand, Supplier shall be rewarded for satisfactory or superior human rights performance. Rewards may include, without limitation, contract renewals, further or expanded orders, contracts of a longer term, investment in increasing Supplier's capacity, or the payment of bonuses. Buyer's evaluation of Supplier with respect to such matters as potential expansion or continuation of the commercial relationship shall give weight to human rights performance [equal] [as well as] to criteria such as quality, price, timely delivery, and the like.

1.4 Grievance Mechanism

During the term of this Agreement, Supplier shall maintain an adequately funded and governed non-judicial Operational-Level Grievance Mechanism (OLGM) in order to effectively address, prevent, and remedy any adverse environmental and human rights impacts that may occur in connection

[31] The term 'agreement' refers to the underlying commercial relationship of which these model clauses are part, and, thus, not only to these model clauses as implemented in this relationship.

with this Agreement or participate in the complaint mechanism of Buyer or in an external (multi-stakeholder) grievance mechanism.

Supplier shall ensure that the OLGM or this external mechanism, if it participates in an external mechanism, is legitimate, accessible, predictable, equitable, transparent, rights-compatible, a source of continuous learning, and based on engagement and dialogue with a reasonable number and/or selection of whistle-blowers and/or affected stakeholders and/or those who have reasonable grounds to believe that they may be affected by a (future) adverse impact, including workers of the Supplier, its subsidiaries and in its supply chain, their representatives, other companies in its supply chain and civil society organizations active in its supply chains in connection with environmental rights or the rights of workers or other affected stakeholders regarding the establishment and functioning of the OLGM on a regular basis.

Supplier shall maintain open channels of communication with those individuals or groups of stakeholders that are likely to be adversely impacted by potential or actual environmental or human rights violations, or which represent these stakeholders and/or whistleblowers, so that the occurrence or likelihood of Adverse Impacts may be reported without fear of retaliation and these individuals or groups and their representatives are informed of the existence and functioning of the OLGM. The Supplier shall uphold a policy to prevent such retaliation, which includes an option for anonymous complaints.

Supplier shall at the Buyers' request demonstrate to the extent allowed by the applicable law that the OLGM is functioning by providing [monthly] [quarterly] [semi-annual] written reports to Buyer on the OLGM's activities, describing, at a minimum, the number and nature of grievances received and processed over the reporting period, documentary evidence of consultations with affected stakeholders, and all actions taken to address such grievances.

Supplier shall ensure that resignation of the right to file a grievance in another mechanism or to commence legal proceedings is not a requirement for access to the OLGM, nor that the use of the OLGM is a prerequisite for the filing of grievances in other mechanisms or the initiation of legal proceedings. Complainants in the abovementioned mechanisms shall be entitled to (a) request an appropriate follow-up regarding the complaint and (b) meet with the Supplier's Representatives at an appropriate level to discuss potential or actual severe adverse impacts which are the subject matter of the complaint.

General Commentary to Article 1

1. Introduction

The Article (as well as the other Articles of these model clauses) is built on the presumption that buyers move from representations and warranties to human rights and environmental due diligence. The reason for this is that two reasons exist to enhance operational effectiveness and enforced legal requirements. For many MNEs there is not much of a risk calculus on this score; simply put, human rights and environmental due diligence is currently required in some European countries (France and Germany) and will likely be required very soon by EU law. Even for MNEs that are not subject to these laws, and for SMEs in similar circumstances, the move still makes sense. Indeed, upon the respect of the specific thresholds established by CSDDD, complying with HREDD duties will be mandatory not only for companies formed in accordance with the law of European countries, but also of non-European countries, when they generate a certain amount of turnover in the EU. The extended scope of application of the Directive makes the requirement to comply with human rights and environmental due diligence very far reaching and the resort to European Model Clauses recommended in a very huge variety of cases. Moreover, Article 22(5) of the CSDDD provides for the overriding mandatory application of the EU Members States' domestic rules introduced in conformity with the Directive and governing the corporate liability for human rights and environmental abuse or damages - with the reasonable implications on contractual issues - even in cases where the law applicable to these claims is the law of a third State pursuant to the relevant private international law rules . Again, this latter provision contributes to expanding the need for companies to conform to the human rights and environmental due diligence duties and following the EMCs within their contracts.

It should be noted that the regime of representations and warranties, with their accompanying liability—if they are not true, there is breach—is unrealistic and ineffective. Frequently, this regime is thought to lead to what is called a "tickbox" or "checkbox" approach to supply chain management in which buyers require a laundry list of representations of compliance from their suppliers. Suppliers mechanistically provide them by checking the boxes (although they may be more than a little resentful of time wasted filling forms).

The participants in the supply chain are no longer being asked, unrealistically and fictitiously, to literally guarantee that no Adverse Impact will occur as well as perfect compliance with the responsible purchasing practices in Schedule Q. Instead, they are being required to undertake due diligence, on an ongoing basis, about achieving those goals. This is not mere aspiration; the parties are contractually obligated to use reasonable means to achieve these goals.

Although the language regarding corporate sustainability due diligence included in the OECD Guidelines or UNGPs is not well suited for contract clauses, the following list provides a good, though not exhaustive, understanding of the concept, which is also aligned with the CSDDD. Human rights due diligence includes:

(i) embedding responsible business conduct into the culture of the company through leadership, incentives, policies, and management systems;
(ii) identifying and assessing actual and potential adverse human rights impacts, throughout the supply chain, that the contract-related activities may cause or contribute to, or that

may be directly linked to the operations, products, or services contemplated by the contract;

(iii) ceasing, preventing, and mitigating such adverse impacts;

(iv) tracking and monitoring, in consultation and collaboration with internal and external stakeholders, the success of mitigation or prevention;

(v) communicating how adverse impacts are addressed, mitigated or avoided; and

(vi) providing for or cooperating in remediation where appropriate.

Effective due diligence requires looking at risks through the perspective of the stakeholder, as learned through engagement with the stakeholder; the prioritization of responsive action by severity of impact on the stakeholder; the need to search on an ongoing basis for human rights risks throughout the entire supply chain, and not just the first few tiers; the development of leverage to influence contractual parties to refrain from, mitigate, or remediate harm to human rights; and the need to go beyond the limits of local law. In other words, human rights due diligence is a necessary part of ongoing supply chain management; it is proactive, forward and backward looking, responsive to actual or potential impacts, and requires meaningful and regular engagement with stakeholders.

2. Section 1.1

(a) The human rights and environmental instruments mentioned in Article 1.1 (a) are not exhaustive. One may also think of relevant UN Human Rights and ILO conventions. Many of them are mentioned in Article 18 of the EU Green Taxanomy[32] and Annexes I and II to the CSDDD.[33] Article 1.1 (a) also refers to other relevant European regulation. One may think of Regulation (EU) No. 995/2010 (Timber Regulation) and Regulation (EU) No. 821/2017 (Conflict Minerals Regulation). Furthermore, it is relevant to see to it that due diligence is commensurate with the draft regulation Com(2022) 453 final on prohibiting products made with forced labour on the Union market.[34]

This collaboration to establish and undertake environmental and human rights due diligence is at the core of this agreement. Therefore, it should be part of the core of the Agreement and not be contemplated for in general terms and conditions or suppliers' codes of conduct.

An Effective Date as mentioned in the heading of this Article may not be necessary, but the parties may prefer an "Effective Date" to be either the date of this Agreement or the date when all conditions which have been set for its coming into force are satisfied. Alternatively, parties may want to set a period during which certain, but not all, obligations under this Agreement are effective. Presumably a certain level of human rights or environmental due diligence will have been done by Buyer before engaging in extensive negotiations with prospective suppliers.

(b) The CSDDD (for example Articles 7(2)(a) and 8(3)(b)), as well as other instruments, such as the OECD Guidelines, put stakeholder engagement at the core of the due diligence process.[35] After all this process is designed to prevent and mitigate Adverse Impacts to these stakeholders (rights

[32] Regulation EU 2020/852.
[33] Com(2022) 71 final, accessible at https://ec.europa.eu/info/sites/default/files/1_1_183885_prop_dir_susta_en.pdf. The amended text can be found at https://data.consilium.europa.eu/doc/document/ST-15024-2022-REV-1/en/pdf.
[34] See also Articles 47-53 of the Battery Regulation EU 2023/1542.
[35] See the OECD Guidelines, II.15.

holders). Therefore, this section implements the obligation of parties in this respect in this agreement.

(c) Large European enterprises have specific obligations to report on their social performance as of 1 January 2023 (and pursuant to article 19a broadened to small and medium sized listed and other larger enterprises as of 1 January 2026).[36] Enhanced specificity of reporting requirements as set forth by Article 19a section 2 (f), for example, includes a description of the human rights due diligence process, of actual or potential adverse impacts identified and any action taken to prevent, mitigate or remediate any actual or potential adverse impacts as well as pursuant to article 19a section 2 (g) a description of the principal risks. According to Considerations 45 and 49 sustainability reporting should include international standards, such as the UNGPs and should also disclose impact of undertakings on people in connection with which dialogue and exchange of views between workers' representatives and a company's management is required and their opinions should also be communicated to relevant administrative management and supervisory bodies pursuant to Recital 50. Consideration 55 also requires that this information should be available in digital format. Furthermore, pursuant to Article 30(1) the information has to be published within 12 months after the balance sheet date. Thus, section 1.1(b) includes the obligation to provide and exchange such information.

However, the section does not allow Buyer to send unspecified 'one size fits all' information requests down the supply chain. The Buyer should only ask for specific information, explain why this information is needed, and should consider the risk of Adverse Impact with this specific Supplier as well as the ability of the Supplier to comply with the request, especially if Supplier is an SME.[37] Furthermore, Suppliers may be reluctant to provide information on their sub-suppliers because they fear to be bypassed by the Buyer.[38] Therefore, it needs to be clarified to them why the information is needed and to discuss with them these justified fears and collaborate to find a solution for this issue.

Thus, the information request should be tailored to the situation of a Supplier. For example, a Supplier may provide information regarding audits of its sub-supplier without mentioning its name or using an intermediary software tool (which does not provide the name to Buyer).[39] Alternatively,

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[36] See COM (2021)189 final, accessible at https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52021PC0189&from=EN, amending Directive 2014/95/EU, which can be accessed at https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014L0095&from=EN. However, article 19c of the draft Directive allows for less specific reporting requirement for small and medium sized enterprises.

[37] Cf. BAFA Guidance ("Zusammenarbeit in der Lieferkette zwischen verpflichteten Unternehmen und ihren Zulieferern - Die wichtigsten Fragen und Antworten für KMU", 1ed June 2023), p. 2, 3, 8, 18 and 19, Accessible at here: https://www.bafa.de/SharedDocs/Downloads/EN/Supply_Chain_Act/guidance_cooperation_supply_chain.html?nn=1469788.

[38] BAFA Guidance ("Zusammenarbeit in der Lieferkette zwischen verpflichteten Unternehmen und ihren Zulieferern - Die wichtigsten Fragen und Antworten für KMU", 1ed June 2023), p. 20.

[39] See BAFA Guidance ("Zusammenarbeit in der Lieferkette zwischen verpflichteten Unternehmen und ihren Zulieferern - Die wichtigsten Fragen und Antworten für KMU", 1ed June 2023), p. 21 and 22.

Buyer may provide tools and financial resources to Supplier to conduct its own assessment of its supply chain.[40]

3. Section 1.2

UN Guiding Principle 13, the 2023 OECD Guidelines for Responsible Business Conduct and existing or upcoming European laws require that businesses avoid causing or contributing to (environmental and) human rights harms through their own activities, address such impacts where they occur, and seek to prevent or mitigate adverse human rights and environmental impacts that are directly linked to their operations, products, or services by their business relationships. Accordingly, this clause seeks to embed obligations to comply with human rights and environmental standards through the entire supply chain. In keeping with the modular approach of these clauses, businesses may want to circumscribe their responsibility in line with the degree to which they are connected to the activities of the business. Two options are given here. One only implements a best effort obligation for the Supplier to implement the same measures as contemplated by the Agreement on its subcontractors. The second option is stricter. It only allows for subcontracting after consent from Buyer (at least for subcontracting above a certain threshold) and with the obligation of result to implement a proper Human Rights and Environmental Due Diligence process. This responsibility of Supplier may in the latter case be emphasized by adding:

> When Supplier acts as a buyer or in a similar capacity in its contracts with subsuppliers or subcontractors, Supplier shall ensure that it complies with all of the buyer responsibilities stated in this Agreement. Such responsibilities include, without limitation, sharing responsibility for HREDD, engaging in responsible purchasing practices as laid out in Schedule Q, and engaging in responsible exit as laid out in Section 1.3(h).

Cascading environmental and human rights due diligence may be challenging or not required if the Supplier has his own code of conduct which is equivalent to that of the Buyer or the most appropriate one to use. The obligation to provide information about the Supplier's own value chain should not be limited to contractual information, but more general to due diligence approaches if an Adverse Impact occurs. All the responsibilities that Buyers assume in this contract, can be assumed by the Supplier in his contract with its suppliers. However, the concept of such obligations of means are clear to practitioners (in Europe), but it may be less clear how they should be achieved and what is exactly expected in practice. Therefore, translating these into the entire supply chain may be challenging and elaboration of the due diligence process further down the supply chain, including which supplier is responsible for which risk, may be helpful. For example, the focus may be on material suppliers and high risk. Furthermore, Suppliers may be reluctant to provide information on their sub-suppliers because they fear to be bypassed by the Buyer.[41] Therefore, it needs to be clarified to them why the information is needed and to discuss with them these justified fears and collaborate to find a solution for this issue.

[40] See BAFA Guidance ("Zusammenarbeit in der Lieferkette zwischen verpflichteten Unternehmen und ihren Zulieferern - Die wichtigsten Fragen und Antworten für KMU", 1ed June 2023), p. 21.
[41] BAFA Guidance ("Zusammenarbeit in der Lieferkette zwischen verpflichteten Unternehmen und ihren Zulieferern - Die wichtigsten Fragen und Antworten für KMU", 1ed June 2023), p. 20.

One should note that the supply chain regarding a specific product may not be linear and may include a 'web' of supplier relationships. Cascading contractual clauses in such supplier webs is challenging, especially where sufficient leverage lacks. In such instances collaboration with business peers, as far as allowed by competition law and as envisaged by Article 7(2)(e) CSDDD, may be of assistance. Engagement in multistakeholder initiatives may be another option. This may render expectations of implementation of Human Rights and Environmental Due Diligence more common in supplier webs. In such supplier webs it is even more important to pay attention to the informational obligations included in section 1.1 to understand the shape of the web. Furthermore, Buyers should realize that they may be supplier as well. For example, if a Buyer sources fabrics from a supplier and sends these to another supplier for garment manufacturing, the Buyer is supplier to the latter and should undertake its own due diligence regarding the fabrics. The due diligence obligations as laid down in Article 1 become more reciprocal in such instances.

The section is commensurate with Article 8(3)(c) of the CSDDD as it requires companies to seek contractual assurances from the partners of their partner with whom they have an established business relationship including appropriate measures to verify compliance.

The content of Schedule P is beyond the scope of this document. Note, however, that some suggest the best practice is to avoid reference to specific laws in favor of a general reference because legislative initiatives are broader in some countries than in others. That said, one may consider referral to Annex I and II of the (Draft) Corporate Sustainability Due Diligence Directive to define Adverse Impact.[42]

The recordkeeping as required by this section may be necessary to meet legislative reporting requirements as under the Corporate Sustainability Reporting Directive. Also UNGP 21 requires businesses to communicate externally, particularly where concerns are raised by affected stakeholders, and sets out standards for the form, frequency, adequacy, and confidentiality of such human rights reporting.

4. Section 1.3

(a) It is not uncommon for buyers to exert their leverage—such as threats of termination—to require discounts or other benefits from suppliers. However, this type of behavior is contrary to the approach implemented in this model. Therefore, this provision is meant to allow supplier to enforce its rights despite any superior leverage that Buyer may have. Buyer is required to satisfy all obligations accrued prior to termination, including payment in full for goods produced without causing or contributing to Adverse Impact. Obviously, this section applies if a Buyer has leverage and is able to 'dictate' the conditions of the agreement. Whether this is the case depends on supply chain dynamics. Such leverage may lack in certain supply chains.

The EU directive on unfair trade practices in agricultural supply chains[43] defines in article 1 section 2 when an imbalance of power occurs between buyer and supplier using differences in turnover as an indicator. This may also be relevant in connection when determining if an SME is involved and how much leverage exists.

[42] Com(2022)71 Final.
[43] Directive EU 2019/633.

Article 7(4) of the CSDDD requires contractual assurances obtained from small and medium sized enterprises to be fair, reasonable and non-discriminatory.

Further guidance regarding the content of Schedule Q (responsible sourcing practices) may be derived from Schedule Q to the ABA MCCs which provides good examples of responsible purchasing practices.[44] One may even consider referring to these practices in the supply chain contract.

One should note that specific requirements apply in agricultural supply chains. The EU directive on unfair trade practices in agricultural supply chains[45] includes further reaching requirements than Schedule Q of the ABA MCCs or requires implementation of certain provisions in Schedule Q of the ABA MCCs. Such unfair trade practices are not allowed in supply chain contracts.[46] Late payments and short-term termination of agreements regarding fungible goods are considered as such, although member states may allow an exemption if these goods can reasonably be sold elsewhere.[47] Beyond this and according to article 3 section 1 under c of the Directive more powerful buyers are not allowed to unilaterally change contractual terms, unless this regards a specific element, such as the agreed quantity, and this has been agreed upon.[48] Beyond this, Article 3(2) of the Unfair Trade Practices Directive in Agricultural Supply Chains, although it does not include explicit provisions on the burden of proof, imposes the burden of proof on the buyer if it desires to implement the provisions mentioned in this section. These provisions are prohibited unless the buyer proves these provisions meet the requirements for an exception to the general rule.

Furthermore, one may consider elaborating Buyer's responsible purchasing practices, which may include providing information to the Supplier from the outset of the relationship regarding projections of order quantities and deadlines as well as the required capacity of Supplier. Such clauses may read as follows:

> (a) From the outset of the commercial relationship, Buyer shall establish a transparent forecasting methodology that results in projections of order quantities and deadlines that take into account Supplier's production capacity and end market demand. To support a high level of accuracy, such methodology shall be based on a sufficient investment in data analysis and demand planning, taking into account relevant geographies, categories, and product designs. Buyer shall share initial and updated forecasts in a timely way to allow Supplier a sufficient time to meet Buyer's revised requirements. Nevertheless, neither forecasts nor projections are binding on Buyer or Supplier unless otherwise agreed.
>
> (b) From the outset of the commercial relationship, Buyer and Supplier shall cooperate to establish the capacity of Supplier to meet the requirements of the Buyer. Such cooperation shall include dialogue between Buyer and Supplier and may also include inspections of

[44] Which can be accessed at https://www.americanbar.org/content/dam/aba/administrative/human_rights/contractual-clauses-project/scheduleq.pdf.
[45] Directive EU 2019/633.
[46] This is especially relevant where an imbalance of power exits. The directive defines in Article 1(2) when an imbalance of power occurs between buyer and supplier through the use of differences in turnover as an indicator.
[47] Article 3 section 1 and considerations 17 and 20 of the directive. However, late payment is allowed if model agreements of approved industry organisations (see Regulation EU 2013/1308) provide for this in connection with specific products. See article 3 section 1 under i) and consideration 19.
[48] See also consideration 21.

records and facilities. The result of this process shall be documented. To the extent that Buyer reserves capacity, Buyer shall pay for it in accordance with the contract or, where there is no contract, in accordance with the Supplier's usual rates.

Beyond this, it is also important to collaboratively set reasonable and achievable deadlines. A clause regarding this may read as follows:

> Buyer and Supplier agree to collaborate to set reasonable deadlines that take Supplier's capacity into account, and the parties shall agree upon deadlines [___] months in advance of production. Such deadlines and other aspects of the timeline shall be renegotiated as necessary to avoid Adverse Impacts that may result from delays, deadlines, or other timing requirements. If Buyer requires that Supplier work with another company, including but not limited to, for supply of materials or services, Buyer shall be responsible for any delay caused thereby.

(b) This section requires Buyer to assist Supplier in implementing Human Rights and Environmental Due Diligence if necessary. If an Adverse Impact has already occurred and even this assistance of Buyer is not sufficient to address an Adverse Impact, this triggers the obligation of Article 2.3 to design and implement a remediation plan.

Parties may consider deeming the cost of reasonable assistance to be a setup or mobilization expense associated with Supplier's preparing to provide goods to Buyer. For example, if Environmental or Human Rights due diligence effectively requires that Supplier make capital improvements to meet targets that may go beyond the minimum requirements of applicable law, Supplier's costs for such compliance may qualify for reasonable assistance from Buyer, especially is Supplier is an SME. Depending on the circumstances, Buyer and Supplier may determine that such assistance should be provided as a single payment at the beginning of the term of the Agreement or the parties may decide to spread assistance over time, over units delivered, or otherwise. Where assistance is provided over time, the parties should clearly state when such assistance might be suspended or whether such assistance would be accelerated on early termination.

If SME suppliers are involved this support is required by Articles 7(2)(d) and 8(3)(e) of the CSDDD. Article 7(2)(d) in connection with Recital 34 of the CSDDD suggest financing, directly or through low-interest loans, as well as guarantees of continued sourcing and assistance in securing financing as potential means to assist suppliers.

It is important to note that a request of a Supplier in the agricultural sector pursuant to Article 3(1)(h) Unfair Trade Practices Directive in agricultural supply chains may not lead to retaliation against this supplier, for example, by reducing or cancelling orders.

(c) This section requires in section (i) that the price paid to a supplier enables it to undertake due diligence and implement necessary measures to enhance the human rights and/or environmental situation.

In line with General Comment 23, para. 18 of the UN Committee on Economic, Social and Cultural Rights (CESCR), living wages are defined as wages "sufficient to enable the worker and his or her family to enjoy other rights in the Covenant, such as social security, health care, education and an adequate standard of living, including food, water and sanitation, housing, clothing and additional

expenses such as commuting costs". Other living wage definitions may be more or less expensive. If Buyer uses another definition, it must be published on the company website and included in relevant policy documents.

Obviously, the Buyer does not (only) want to increase the supplier management remuneration, but also desires to have the required measures implemented, for example payment of a living wage to workers. Therefore, it is not sufficient to just pay a higher price for the goods delivered. The Buyer should also contract for measures to safeguard and assess whether the additional funds paid are used to implement the required measures. External assurance may be a viable option to assess this.

It should be noted that incentives for Suppliers to undertake due diligence may be implemented other than paying a higher price may be implemented. For example, more orders or continuation of a longer lasting relationship may be such incentives. Another important way to achieve this is through collaboration with business peers and undertaking environmental and human rights due diligence a common expectation of multiple buyers.

Initially, parties may focus their efforts on countries with particularly high poverty rates and low or non-existent minimum wages. Although not required by this model agreement parties may consider to implement a living wage or at least strive to work towards a living wage.[49] That said, the minimum wage should be the starting point. See in this regard also Annex I (points 7 and 17) of the CSDDD which includes the requirement to provide for a living wage. In exceptional circumstances the minimum wage may be higher than a living wage. In such instances the minimum wage should be the standard.

A more extensive pricing clause may be considered as well. It could read as follows:

> (1) Buyer and Supplier shall collaborate to agree on a price that accommodates the costs associated with upholding responsible business conduct in accordance with 1.1, including the payment of the applicable minimum wage or a living wage, whichever is higher. If the payment of a living wage is not immediately feasible, then Buyer and Supplier shall commit to a progressive, evolving pricing schedule to pay a living wage within a reasonable time.
>
> (2) If unforeseen and material increases in input prices, including wages, would cause Adverse Impacts, Buyer and Supplier will collaborate to agree to alternative terms (by way of illustration, price adjustment, advance payment, schedule changes, extended contract term) to avoid such impacts. If the parties cannot agree, the matter shall be referred to dispute resolution as provided by Article 7.
>
> (3) At all times, Supplier must be able to document that it is using the price protections in this section to comply with 1.1. Buyer shall have the right to request and inspect this documentation. If Supplier has not used the resources provided in an appropriate manner, Buyer may reclaim them.

The second part of this section (ii) is connected with a material increase of cost of materials used to produce the Good. Especially if Suppliers is a SME's this may trigger Adverse Impacts if it must continue production on the agreed prices. It may, for example, lead to an abuse of workers by demanding excessive overtime to produce more goods within a shorter timeframe in order to

[49] See also the OECD Guidelines V (Employment and Industrial Relations), V.4.b.

compensate for the increased sourcing prices. This section provides for a collaborative approach regarding this issue. In cases where a Buyer lacks leverage to 'dictate' contractual terms or the Supplier is a large entity itself, it may be less necessary to implement this section.

(d) If specifying the terms mentioned is not commercially feasible at the outset, the parties may agree that they will specify them at a later stage, in full accordance with this section, in order to avoid causing or contributing to Adverse Impacts.

(f) Excusable non-performance may, for example, occur if a supplier lacks sufficient personal protective equipment (PPE) to protect its workers in a pandemic to allow for normal operations. This section is intended to address not only change orders but force majeure-like events that go beyond a simple change in conditions affecting a single supplier.

(h) Human rights remediation should not build on termination as current contractual mechanisms often do. However, usually parties would not actually move to termination except in the rarest and most egregious circumstances.[50] Beyond this, termination often worsens the human rights or environmental situation.[51] Therefore, this section requires remediating the problem by taking measures to stop and correct the harm and to address any grievances. Termination usually is in no one's interest. The buyer does not want to suffer the disruption and incur the delay or switching costs to transfer its business to new suppliers. The supplier certainly does not want to lose business. And except in the most extreme circumstances, the workers do not want to lose their jobs and their livelihood.

Article 8 CSDDD and Recital 32 confirm that companies should continuously engage with their business relations and disengagement is a measure of last resort. Recital 36 also allows prioritizing engagement with business relationships in value chains instead of termination as a last-resort action after unsuccessfully attempting to prevent and mitigate adverse impacts. If the adverse impact cannot be brought to an end Article 8(6) of the proposal and Recitals 36 and 41 also refer to the obligation to refrain from entering into new or extending existing relationships in such instance and, as far as allowed by the applicable law, suspend commercial relationships if it is expected to be successful on the short-term or terminate if the potential impact is severe.

In cases where it is not possible to bring to an end or mitigate all identified Adverse Impacts simultaneously, companies may prioritize the order in which they take appropriate measures. They should do so on the basis of the severity and likelihood of impacts and in a manner informed by meaningful engagement with affected stakeholders.[52] The severity of an Adverse Impact should be determined based on its gravity, the number of individuals that are or will be affected, or the extent of the damage or potential damage to, or other effects on, the environment, whether the impact is irreversible and any limits on the ability to restore affected individuals or the environment to a situation equivalent to their situation prior to the impact. The company's degree of influence,

[50] See also Recital 36a CSDDD. See also the commentary to the OECD Guidelines to II (General Policies), para. 25, See also the OECD Guidelines V (Employment and Industrial Relations), V.6.
[51] See also Recital 41a CSDDD.
[52] See also Recital 26a CSDDD.

leverage over or proximity to the subsidiaries or entities with which it has a business relationship should be considered to be less relevant to its prioritization decisions.[53]

Section 1.3(b) also applies to the responsible exit. Buyer may have to provide support to prevent additional Adverse Impacts and bear part of the cost made by Supplier if Supplier is an SME or, pursuant to Article 5.2(e), if Buyer has caused or contributed to the Adverse Impact.

(i) Many Suppliers have multiple Buyers. Oftentimes these Buyers have implemented their own Human Rights and Environmental Due Diligence process including questionnaires, audits and scorecards. If the Supplier has to fill in all these questionnaires and has to accept multiple audits (for which it usually also has to pay), this is a heavy burden. This section aims to alleviate this burden by implementing recognition of (comparable) questionnaires or audits for other Buyers.

An equivalent document as referred to in this section is, for example, a questionnaires completed for another buyer or an audit reports prepared by a reputable third-party.

(j) Positive incentives for Supplier to implement and undertake proper Human Rights and Environmental Due Diligence may be even more productive than sanctions. This section provides for such positive incentives. It may be further elaborated depending on the type of supply chain and assessment of effective positive incentives.

5. Section 1.4

This section is aligned with the UNGPs as an "operational level grievance mechanism" is set up to address problems as they arise. This mechanism is informal, but it is nevertheless required, and it must be fully functional. Again, its purpose—to be "legitimate, accessible, predictable, equitable, transparent, rights-compatible, a source of continuous learning and based on engagement and dialogue with affected stakeholders, including workers"—will align with many companies' efforts toward collaborative supply chain management. Further, it is required for consistency with the UNGPs.

UNGP 29 provides that all businesses must have in place a grievance mechanism to resolve human rights disputes early and directly through engagement and dialogue with stakeholders. It is part of the businesses' ongoing HRDD responsibility. UNGP 22 expects that businesses should cooperate with or participate in legitimate remedial processes when the businesses recognize that they have caused or contributed to an adverse impact. Legitimate processes can include state judicial and non-judicial dispute resolution mechanisms, as well as non-state non-judicial mechanisms. Under UNGP 31, all non-judicial dispute resolution mechanisms, state and non-state, should meet the effectiveness criteria enumerated in the text of the clause.

The Article as such does not provide much guidance, except for the referral to UNGP 31, regarding the question how an effective grievance mechanism should look like. The EMCs are not the right place for this. Buyers and supplier should consult experts or relevant institutions for such guidance. That said, a few observations are made. It is important to assess for which stakeholders and which type of complaints the mechanism is intended and to consult relevant stakeholders on the design

[53] See the new paragraph 2a to Article 8 CSDDD proposed by the European Parliament, 2022/0051(COD), p. 77. See also Article 6a CSDDD.

and functioning of it.[54] However, it should not be overly restrictive in identifying the relevant stakeholders and type of complaints. Buyers and suppliers may consider stakeholder or community driven or multi-stakeholder mechanisms as an alternative.[55] One should also consider how to prioritize complaints if very many are filed in the mechanism. Finally, it is important stakeholders are aware of the mechanism and have meaningful access to it. For example, upfront signing away of rights to engage in other mechanisms should not be a requirement for access. Furthermore, it is important to protect complainants from retaliation, for example, by allowing anonymous complaints and establishing a safe and secure environment to file complaints. Finally, if every buyer of a specific supplier asks for its own mechanism or sets forth its own requirements, this may be counterproductive not only in terms of the burden this implies for the supplier to maintain many different systems but also in terms of accessibility for rights holders who may not know which mechanism they should use, for example because they are not aware for which buyer they are producing or because they do not trust a mechanism of which they do not know in which manner their complaints are handled and whether and to which extent information regarding claim is shared with the Supplier. Therefore, it is advisable to collaborate with other buyers to establish one or strengthen an existing mechanism at the supplier level. In establishing their mechanisms Buyer and Supplier should pay attention to existing mechanism, such as local mechanisms operated by third parties (NGOs), OECD NCPs or mechanisms established by other buyers. Duplication of mechanisms should be prevented to the extent possible.

Buyers should assist in establishing such mechanisms at the supplier level, amongst other things, depending on the size of the supplier. The smaller a supplier is, the more support should be provided, also in financial terms. Alternatively, Buyer may consider establishing its own mechanism and assist Supplier in making it accessible for affected rights holders at the Supplier level. However, OLGMs at local level are usually easier accessible than the more remote mechanism at the Buyer level. For example, workers at the supplier level may not be aware for which buyer they are producing and consequently may not know which mechanism at the buyer level they should use.

[54] See also Recital 26a CSDDD.

[55] Cf. BAFA Guidance ("Zusammenarbeit in der Lieferkette zwischen verpflichteten Unternehmen und ihren Zulieferern - Die wichtigsten Fragen und Antworten für KMU", 1ed June 2023), p. 33.

Practical Guidance to Article 1

Section 1.1

(a) Article 2(m) of the Conflict Minerals Regulation includes a specific provision on certification. A certification scheme may be approved by the European Commission if it meets the OECD due diligence guidance and pass the OECD alignment test. The presumption of undertaking sufficient human rights due diligence may be inferred from the engagement in or implementation of an (approved) certification scheme or designated multi-stakeholder initiative is implemented by small or medium sized enterprises.

Technical solutions like blockchain may support establishing and maintaining an environmental and human rights due diligence process, although the blockchain does not itself assess the Human Rights or environmental situation. Blockchain may require that Human Rights and environmental compliance is checked before data may be fed into the blockchain. It is already used by companies to enhance traceability of goods.

(c) To determine an appropriate living wage, parties may consult www.globallivingwage.org, wageindicator.org. or other leading industry benchmarks and data sources relevant to the specific sector(s). Living wage estimates must be updated at least annually. If they provide data in accordance with the definition of living wages. If no reference values are available, the salary can be determined according to a method approved by IDH trade, available at: https://www.idhsustainabletrade.com/idh-living-wage-identifier/. Another method is developed by the UN Global Compact and may be accessed at https://livingwagetool.unglobalcompact.org/.

(h) The former Bangladesh Accord (currently: International Accord) provided some additional guidance on responsible exit.[56] It included three stages. First a letter should be sent to the supplier management to inform it, it is in breach of the remediation plan and to give a specified number of days to bring about specified improvements, if these are implemented no further steps are necessary. If not, the management of all the brands sourcing from the factory send a warning letter to the supplier, stating that if the steps specified in the remediation plan are not taken within a specified number of days these brands are legally required to terminate the relationship. At this point the Accord Secretariat, the supplier and the brands to explain how disengagement should proceed, if necessary, and to determine whether additional financial commitment from the brands is required. The third step is responsible disengagement if the requirements of the remediation plan are not met within the specified time. This implies collective disengagement by all Accord brands. However, the brands are still responsible for compensating workers for termination of work resulting from disengagement, but no longer for other cost. This implies, for example, that the disengaging brands are expected to temporarily pay workers' salaries, and the brands have to make reasonable efforts to find alternative employment for the workers as the working environment is unsafe in such cases. This is especially important for union leaders who may have pointed at the issue and may be blacklisted. Blacklisting results in difficulty in finding future work. In such cases the Accord may also intervene. The supplier then remains blacklisted for 24 months and may reapply after that. That said, in case of acute fire or building danger the escalation protocol may be skipped

[56] The Bangladesh Accord 'escalation protocol' for responsible engagement and disengagement. See on this OECD Watch, Legislating due diligence: Respecting rights or ticking boxes?, p. 26, accessible at https://www.somo.nl/respecting-rights-or-ticking-boxes/.

and a buyer may immediately move to disengagement. This is an interesting example as it uses collective leverage of buyers sourcing from a specific facility to increase the credibility and eloquence of the threat of disengagement, which is a more powerful instrument than such a threat expressed by a single buyer. This is not a feature which as such can be included in model supply chain contracts, but it can be part of multi-stakeholder initiatives and collaboration between buyers to increase leverage. It should also be noted that disengagement does not terminate responsibilities of the buyer towards workers, especially regarding their compensation and, if applicable, reasonable efforts to find alternative employment for them. Beyond this, a model contract may include a provision stipulating that the buyer will not reengage with the supplier during a specified period of time, for example, 24 months. This also increases the threat of disengagement. It is to be expected that European multi-stakeholder initiatives, such as the Dutch International Responsible Conduct Agreements and the Fair Wear Foundation, may consider and implement this disengagement approach as a best practice.

Section 1.4

To protect complainants against retaliation, one may find relevant guidance in legislation aiming at whistleblower protection, such as Directive (EU) 2019/1937 (Whistle-blower Directive) as well as legislation governing this matter on member state level. One should also note Directive (EU) 2016/943 (Trade Secrets Directive), which provides further guidance on the issue.

Procedural rules have also been developed to protect against retaliation in (arbitral) proceedings. These may serve as an example. One may look at Articles 18(5), 33(3), 38(2)(c), 41(2) and 42(2)(a) of the Hague Rules on Business Human Rights Arbitration[57] and Articles 23(3), 24(4) and 39-41 of the procedural rules of the dispute resolution mechanism of the Dutch International Responsible Business Conduct Agreements in the Textile sector.[58]

[57] Accessible at https://www.cilc.nl/cms/wp-content/uploads/2019/12/The-Hague-Rules-on-Business-and-Human-Rights-Arbitration_CILC-digital-version.pdf.

[58] Accessible at https://www.imvoconvenanten.nl/en/garments-textile/agreement/-/media/3670C016696D4456A9AB82DEAD9E88E4.ashx. See also https://www.ser.nl/en/themes/irbc/complaints-disputes-committee for the decisions of this mechanism. The International Responsible Business Conduct Agreement in the Natural Stone sector includes comparable instruments in Articles 10(4), 23(3), 24(4), 26(3) and 39-41. These rules are accessible at https://www.imvoconvenanten.nl/en/trustone/initiatief/-/media/5EEE6797C4A846F39A6A7EC0818B8A31.ashx.

Member State specific comments to Article 1, UK and DCFR

1. France

Section 1.1: One should bear in mind that due diligence in France should include a Vigilance, Transition and Remediation plan.

Section 1.3: One should assess whether this clause is commensurate with Article L.442-6 of the Code de commerce.[59] By and large such collaborative contracting is in line with French law.

2. Germany

Section 1.1(a): At least in constellations in which buyers are large firms and suppliers are SMEs the requirements of the BAFA Guidance ("Zusammenarbeit in der Lieferkette zwischen verpflichteten Unternehmen und ihren Zulieferern - Die wichtigsten Fragen und Antworten für KMU", 1ed June 2023)[60] does require more specific provisions on the exact roles both parties have in the exercise of certain due diligence obligations. This could also be argued in other constellations where suppliers are not obliged under human rights and environmental due diligence, especially if they have limited capacity. For example, SMEs might not be expected to do their own full scale risk analysis but could rather rely on information given to them by buying firms and collaborate in buyer`s risk analysis as requested. This could also be derived from the LkSG requirements on adequacy and effectiveness, as well as under the reasonableness requirement that applies for the use of standard terms (Sec. 307).

Section 1.1(b): Business practice in Germany is using annual questionnaires to a risk-based selection of suppliers as regular information channel and ad hoc requests for specific risk situations. The buyer might also be required to take a cooperative approach on this, amongst others, accepting other standard questionnaires and scorecards that suppliers might have filled out ("Once-only") and that include the relevant information on their risk situation to avoid over-bureaucracy.

Section 1.2: This section may enable the buyer to retrieve information regarding the supplier`s suppliers which may enable it to exclude the supplier by making direct contracts with the supplier's suppliers. This may render the clause void under German Law under the General Terms and Conditions Law and may create an incentive for suppliers to not conclude contracts. In order to make this clause commensurate with German law one may consider a cooling off period in which the buyer is not allowed to contract with a supplier`s suppliers or other types of safeguards, like giving the supplier the right to propose disclosure to trusted third parties as clearing.

Section 1.3: These provisions have a very high relevance for fulfilling the obligations on responsible purchasing under Sec. 6 (3) No. 2 LkSG. It should be noted that the usage of this clause might not be required under LkSG in situations of power imbalances between small buyers and big buyers.

Section 1.4: Monthly or quarterly reports are likely to be considered too burdensome and potentially inadequate for suppliers, especially SMEs under Sec. 307 of the German Civil Code, if not justifiable

[59] As modified by the loi Hamon du 17 mars 2014.
[60] Accessible at here: https://www.bafa.de/SharedDocs/Downloads/EN/Supply_Chain_Act/guidance_cooperation_supply_chain.html?nn=1469788.

by a very high risk situation of the supplier - if a supplier has many buyers, this provision would require them too very burdensome and time-intensive reporting.

Furthermore, the German Supervisory authority BAFA requires Buyers to implement their own grievance mechanism. BAFA considers a mechanism at the Supplier level optional. This implies, where supplier is not obliged by LkSG, LdV, Norwegian Transparency Act or similar, requiring them only to participate in Buyer`s mechanism and alternatively establishing their own mechanism or participating in an external one, if these alternatives meet the requirements of Sec. 8 LkSG / UNGP 31.

3. Italy

Section 1.1: As far as Italian data protection rules are concerned, in addition to the GDPR, the matter is governed by the Italian privacy code, which is Legislative Decree No. 196 of June 2003; the Parties might wish to refer to this legislation in the contract and will have to ensure compliance of the due diligence process with such rules.
Section 1.3: Under Italian law (articles 1337 and 1375 of the Italian Civil Code), in the negotiation phase and during the drafting and the performance of the agreement, the parties shall act in good faith. The violation of such good faith obligation may give rise to contractual liability of the defaulting party, and an obligation to pay damages as a consequence. Buyers should consider such Italian provisions especially with regard to section 1.3(d) (*Modifications*) and section 1.3(f) (*Responsible Exit*).

Furthermore, and unless specifically approved in writing by means of a double signature (*doppia sottoscrizione*), general terms that establish, in favor of the party which drafted them, limitations of liability, the right to withdraw from the contract or suspend its execution or provide for the other party the penalty of forfeiting rights, limitations on the right to oppose exceptions, restrictions on contractual freedom in dealings with third parties, tacit extension or renewal of the contract, arbitration clauses or exceptions to the jurisdiction of the judicial authority, are not valid under Italian law.

While the concept of 'commercially reasonable efforts' (as opposed to best efforts/reasonable best effort or other similar concepts) is sufficiently defined in certain jurisdictions, corresponding precise standards do not exist in the Italian legal system, which mostly differentiate between so-called obligations of means (*i.e*. also known as obligations of diligence, which consists in the diligent use of the means at debtor's disposal to perform a certain activities without ensuring the final result (*e.g.,* the obligations of a lawyer in court) and obligations of result (the debtor undertakes to achieve a specific result)). Therefore, the parties might rely on such language, (*e.g.*, the Supplier/Buyer undertakes to take all necessary steps in order to […] / undertakes to diligently pursue…) although the precise scope of such obligation may vary depending on the specific circumstances.

4. Poland

Section 1.2: Polish contract law is obviously based on the principle of privity of contracts, but this does not prevent one party from promising the other that it shall enter into certain contractual

relationships with third parties or from guaranteeing that certain third parties will act in a certain manner.

Section 1.3: Buyer's obligations as envisaged by this clause add balance to the contractual relationship. Removing them may create the risk of the contract falling foul of legislation aimed at preventing abuses of contractual power (such as e.g. the Polish Act on countering unfair use of contractual power in trade of agricultural and food products).

5. Portugal

One should be aware that the collaboration as envisaged by Article 1 does not to violate Law 19/2012, of 08 May (Portuguese Competition Law), notably Article 9 on Agreements, concerted practices and decisions by associations of undertakings, Article 11 on Abuse of a dominant position and Article 12 regarding Abuse of economic dependence.

Section 1.1: One should bear in mind Article 406(2) of Decree-Law 47344/66, of 25 November (Civil Code)[61] on the effectiveness of contracts.

Section 1.3: Portuguese law foresees a set of limitations concerning general contractual clauses drafted without prior individual negotiation, which tenderers or undetermined addressees limit themselves to subscribing or accepting, respectively, as well as concerning clauses inserted in individualised contracts, but whose previously prepared content the addressee cannot influence.

It should be safeguarded that a party to an agreement cannot use its leverage to push for disproportionate commitments and rights where the other party did not have the opportunity to negotiate the terms of the agreement at hand.

Notably, the following general contractual clauses are always null and void:

- Clauses contrary to good faith;
- Clauses that directly or indirectly exclude or limit monetary damages arising from tort;
- Clauses that directly or indirectly exclude or limit contractual liability in case of fraud or wilful misconduct;
- Clauses that exclude termination of the agreement by breach.

The burden of proof regarding a contractual clause which has originated from prior negotiation between the parties (and, thus, is not null and void) falls upon whoever intends to take advantage of its content.

In this context, to the extent that the terms of the model clauses may be imposed with little to no negotiation from the counterparty, and to the extent that the model clauses trigger any of those forbidden clauses (e.g., by rendering termination of the agreement too cumbersome and, thus, in practice excluding it), they are null and void.

[61] Accessible at DL n.º 47344/66, de 25 de Novembro (pgdlisboa.pt)https://www.pgdlisboa.pt/leis/lei_mostra_articulado.php?nid=837&tabela=leis&so_miolohttps://www.concorrencia.pt/sites/default/files/documentos/legislacao/Law_19_2012_bilingual_en_0.pdf.

See regarding this also Decree-Law 446/85, of 25 October (General Contractual Clauses Regime)[62] and notably Articles 18 (Clauses prohibited in all cases) and 19 (Clauses prohibited in certain circumstances).

6. Spain

Section 1.1(b): Directors (*administradores*) are subject under Spanish Corporate Law to a specific regime (Chapter III) which protects their independence of judgement when carrying out their fiduciary duties in the interest of the company and which can be inconsistent with the reference of either the Buyer and/or Supplier causing their directors (as Representatives) to discharge the obligations contemplated in this Article 1.1(b); we suggest deleting the reference to "directors".

As regards the content of the "qualitative and quantitative" information to be provided by the Supplier to the Buyer, to the extent that Buyer and Supplier could be actual or potential competitors in a market (which might be the case especially in no linear supply relationships), due attention should be paid to avoid any exchange of information which could be commercially sensitive according to the relevant antitrust laws and regulations, basically meaning information which may influence the way the Buyer or the Supplier would act in such particular market, as this may amount to a breach of Article 1 of Spanish Antitrust Law 15/2007 of 3rd of July and/or Article 101 of the Treaty on the Functioning of the European Union. To further prevent any potential antitrust breach in those cases where Buyer and Supplier may be competitors, clean teams may be set up to exchange any sensitive information which might be necessary to the human rights and environmental due diligence process.

The Spanish and European provisions on data protection must also need to be taken into account to implement the proper security mechanisms in the event that the anticipated exchange of information involves personal data.

Section 1.2: The concept of "best effort" (or "commercially reasonable efforts" as used in Article 1.3(b)) qualifies under Spanish law as an undefined legal concept ("*concepto jurídico indeterminado*") which shall be interpreted taking into account the circumstances surrounding the discharge of the obligation. It must be bore in mind that according to Spanish case law this clause could also be interpreted as creating an obligation of result, and not of means.

Section 1.3(a): The concept "fair", as it is drafted in this Article, can be interpreted in very broad terms under Spanish law and, therefore, can be potentially troublesome. As the Spanish Civil Code already contemplates in article 1546 that all contracts must be discharged in good faith, we would suggest to delete the reference to this term ("fair").

Section 1.3(c): If Buyer and Supplier are actual or potential competitors this clause is especially sensitive in the sense indicated in our comment to Article 1.1(b). On this account the parties may decide not to include it or set up a clean team to manage it.

Section 1.3(g): the wording of this clause may introduce an excessive uncertainty about the enforceability of the contract and the rights of the parties and in this sense it would be advisable to

[62] Accessible at DL n.º 446/85, de 25 de Outubro (pgdlisboa.pt)https://www.concorrencia.pt/sites/default/files/documentos/legislacao/Law_19_2012_bilingual_en_0.pdf.

introduce an element of objectivity in its application like, for example, deferring to the assistance of a third party opinion on the possibility of its triggering.

Furthermore, contractual parties should be aware that contractual terms establishing limitations on contractual liability are not enforceable in the event of wilful intent ("*dolo*").

Section 1.3(h): Further to article 1255 of the Spanish Civil Code (the parties in a contract can agree on anything which is not contrary to law, morals or public order) a clause limiting or conditioning the termination rights of the Buyer is allowed. Notwithstanding this, it must be noticed that since 2016 the Spanish Supreme Court sustains that general terms and conditions of contracts ("*condiciones generals de la contratación*") amongst entrepreneurs (*"Empresarios"*) must be consistent with the principle of good faith, implying that in the future the Spanish courts could analyse the content of such clauses and modify it, altering the balance of rights and obligations amongst the contractual parties.

7. UK

Section 1.3: The concept of "commercially reasonably efforts" does not have a clear or settled meaning under English law; given that this term is used in context of Buyer's obligations it is suggested considering replacing this with the more commonly used "reasonable endeavours" or "reasonable efforts".

8. Draft Common Frame of Reference (DCFR)[63]

Section 1.3: seems also to be commensurate with principle 43 of the DCFR that one may not take undue advantage of the (economic) position or lack of expertise of the other party.

(a) This section may also serve to satisfy the demands of Article II-9:105 regarding grossly unreasonable contract prices determined by one party and to prevent unfair standard terms between business as referred to in Article II-9:405.

(f) This section may be suspect under Article III-3:105(2) if non-termination would violate good faith and fair dealing. However, it is expected that this would rarely happen. It may also be contrary to Article III-3:502 if non-performance is fundamental, which may be the case regarding human rights violations. However, one may argue this section in the EMCs is connected with providing the supplier a period of time to cure the non-performance, which is allowed under Article III-3:202. Furthermore, one should realise that the occurrence of an Adverse Impact as such does not implicate a breach of this Agreement. This will be the case only if this would result from deficient Human Rights and Environmental Due Diligence as required by this Agreement or when one of the parties fails to implement remediation measures as required by this Agreement.

[63] Accessible at https://www.law.kuleuven.be/personal/mstorme/2009_02_DCFR_OutlineEdition.pdf.

Article 2 Remediating Adverse Environmental and Human Rights Impacts Linked to Contractual Activity

2.1 Detailed summary of Potential or Actual Adverse Impacts

(a) Within _____days of (i) Buyer having reason to believe and informing Supplier there is any potential or actual [Severe] Adverse Impact, or (ii) receipt of any oral or written notice of any potential or actual Adverse Impact, Supplier shall provide to Buyer a detailed summary of (1) the factual circumstances surrounding such impact; (2) the specific environmental or human rights issues implicated; (3) the investigation and remediation that has been conducted and/or that is planned as informed by implementation of the grievance process set forth in Section 1.4. Buyer is legally bound to disclose this summary as required by law.

(b) Supplier hereby designates (name) (title) at (email address) and Buyer designates (name) (title) at (email address) to send/receive all notices provided under this Section 2.1 and Section 2.3 [and in addition notices shall be given as specified in Section ____ for general notices under this Agreement].

2.2 Investigation

(a) Upon receipt of the detailed summary under Section 2.1, Buyer and Supplier shall to the extent legally allowed fully cooperate with any investigation by the other party or their representatives. Without limitation, such cooperation shall include, upon request of a party, working with governmental authorities to enable both Supplier and Buyer or their agents to enter the country, to be issued appropriate visas, and to investigate fully. If Supplier is a SME and a third party is engaged to conduct the investigation, Buyer shall bear the cost of this investigation.

(b) Each party shall provide to the extent legally permitted the other with a report on the results of any investigation carried out under this Section; provided that any such cooperation in the investigation does not require Buyer or Supplier to waive attorney-client confidentiality, nor does it limit the defenses Supplier or Buyer may raise.

2.3 Remediation of Adverse Impacts

(a) This section applies if a party (the “Non-Connected Party”) forms the view that the other party (the “Connected Party”) has caused or contributed to an actual Adverse Impact. For purposes of this Agreement, a party can be deemed to have contributed to an actual Adverse Impact if it violated Articles 1.1-1.3 and such violation was a significant contributing factor to the actual Adverse Impact in question.

(b) If this clause applies, the Non-Connected Party shall notify the Connected Party of the following matters:

(i) that the Non-Connected party has formed the view that the Connected Party has caused or contributed to an actual Adverse Impact;

(ii) reasonable details of the actual Adverse Impact; and

(iii) that the Connected Party must prepare and implement a remediation plan (the “Remediation Plan”) in accordance with this clause.

(c) In the event that both parties have caused or contributed to the same actual Adverse Impact, and each party provides the other party with a notice under the preceding clause, then each party:

(i) will be a Connected Party with respect to its own involvement in the actual Adverse Impact, and a Non-Connected Party with respect to the other party's involvement in the actual Adverse Impact; and

(ii) agrees that it will cooperate with the other in good faith to satisfy all the requirements of this clause.

(d) Upon receiving notice, the Connected party shall prepare, and submit to the Non-Connected Party within [___] days, or such other timeframe as agreed, a Remediation Plan, which shall:

(i) be designed to ensure that the affected stakeholders, including those who have filed a complaint regarding the Adverse Impact in the mechanism referred to in Article 1.4, are, to the extent possible, put in the position they would have been in had the actual Adverse Impact not occurred;

(ii) enable remediation that is proportionate to the actual Adverse Impact, which may include apologies, restitution, rehabilitation, financial and non-financial compensation, as well as prevention of additional Adverse Impacts;

(iii) indicate the steps that the Connected Party proposes to take (the "Remediation Steps") to:

(A) assess its connection to the actual Adverse Impact;

(B) remedy the actual Adverse Impact in accordance with (d)(i) and (d)(ii) above;

(C) develop or use its leverage over any third parties that are also connected to the actual Adverse Impact to influence the third parties to remedy their own involvement in the actual Adverse Impact;

(iv) include a timeline for the completion of the Remediation Steps, to be agreed between the parties;

(v) include quantitative and/or qualitative indicators for determining when the Remediation Steps are completed; and

(vi) include a timeline to prepare and publish one or more written [public] reports on the Remediation Plan implementation.

(e) The Connected Party shall take all reasonable steps to implement the Remediation Plan within the timeframe agreed between the parties and provide to the Non-Connected Party reasonably satisfactory evidence of the Remediation Plan's implementation.

(f) The Connected Party shall demonstrate to the Non-Connected Party that affected Stakeholders and/or their representatives [and/or a third party acting on behalf of such Stakeholders] have participated in the development of the Remediation Plan and are being regularly consulted in the implementation of the Remediation Plan.

(g) Before the Remediation Plan can be deemed fully implemented, the Connected Party shall provide evidence that affected Stakeholders [and/or their representatives] have participated in

determining that the Remediation Plan has met the standards developed under this clause. Where applicable, such evidence shall include verification that the Remediation Plan has been implemented in a manner that is reasonably satisfactory to the adversely impacted Stakeholders.

(h) Article 1.1 (b) applies regarding any engagement with Stakeholders and/or their representatives [and/or a third party acting on behalf of such stakeholders].

(i) The Non-Connected Party shall provide reasonable assistance to the Connected Party in preparing and implementing the Remediation Plan, which may include, to the extent reasonable, in-kind contributions, capacity-building, and technical or financial assistance.

(j) A failure by the Connected Party to prepare, or properly implement, a Remediation Plan is a material breach of this Agreement, and the Non-Connected Party shall have the right to exercise its remedies, including termination. If the Non- Connected Party elects to terminate this Agreement, it shall do so in accordance with Section 1.3(h) on responsible exit.

(k) If the Adverse Impact has occurred at the level of a supplier or subcontractor of Supplier and if either Supplier or Buyer have become aware of this Adverse Impact, Supplier shall require its supplier or subcontractor to prepare a Remediation Plan to which sections 2.3(b)-(i) of this agreement apply. If the Adverse Impact has occurred in the supply chain beyond the supplier or subcontractor of Supplier level, Buyer and Supplier shall collaborate, after they have become aware of this Adverse Impact, to exercise leverage over the entity where the Adverse Impact has occurred to the extent possible and incentivize prevention, mitigation and remedying the Adverse Impact.

(l) The Remediation Plan may include the termination of an agreement or affiliation of Supplier with a specific factory, termination of a subcontract or removal of an employee or employees and/or other Representatives as far as and to the extent allowed by law if the Adverse Impact cannot be remedied by implementing other due diligence measures as referred to in Article 1.1(a) and which the relevant factory, subcontractor, employee or Representative has caused or to which the relevant factory, subcontractor, employee or Representative has contributed. Article 1.3 (h) applies to this termination.

(m) For the avoidance of doubt, to the extent the actual Adverse Impact results from a Human Rights and Environmental Due Diligence related breach, both this Clause and Article 5 shall apply. A Remediation Plan under this Article 2.3 shall be a fully binding part of this Agreement.

2.4 Excess of Cure Period or Impossibility of Cure

If a severe Adverse Impact is not cured or adequately minimized within the period designated under Section 2.3(d)(iv) or is incapable of being cured, Buyer may in accordance with section 1.3(h) terminate this Agreement if Buyer has not contributed to the Adverse Impact and the Adverse Impact is caused or contributed to by Supplier. If the previous condition for termination is not met, parties shall negotiate in good faith in order to find a solution to address the Adverse Impact. If they fail to reach a solution, the dispute resolution mechanisms set forth in Article 7 will apply.

2.5 Right to Immediate Termination

Notwithstanding any other provision of this Agreement, this Agreement may be immediately terminated by Buyer under 5.2(e), without providing a cure period as referred to in Section 2.3(d)(iv), if Supplier has engaged in a Zero Tolerance Activity to which Buyer has not contributed. A

“Zero Tolerance Activity” shall be any of the following activities if they were not disclosed promptly by Supplier to Buyer during due diligence under Section 1.1(a) activities that would expose Buyer to criminal liability . Such termination shall be effectuated in compliance with Section 1.3(h) on responsible exit. Buyer shall not source with Supplier for a period of at least two years after a termination under this section.

General commentary to Article 2

1. Introduction

Because everyone should contemplate remediation of Adverse Impacts in almost all circumstances, this Article provides for remediation. In addition, remediation is not solely the responsibility of the Supplier; the Buyer must participate if it has caused or contributed to the problem. These provisions are not only in keeping with the shared responsibility of buyers and suppliers but also seem especially appropriate in cases where the buyer has caused or contributed to the harm.

It is important to realize that the occurrence of an Adverse Impact will not automatically imply a breach of the Agreement. For example, Buyer and Supplier may have implemented sufficient Human Rights and Environmental Due Diligence but may not have prevented an Adverse Impact further down the supply chain. Furthermore, an Adverse Impact at the Supplier level may also be contributed by the Buyer and, thus, may not be a (sole) breach of the Supplier. Therefore, this Article does not frame Adverse Impacts as such as a breach of the Agreement but sets forth that a remediation plan has to be established and implemented (within the cure period) if the Adverse Impact cannot be cured right away. Obviously, a breach may occur, for example if Buyer or Supplier have not undertaken Environmental or Human Rights due diligence in accordance with Article 1.1 or when Buyer or Supplier does not comply with Article 2. However, remedies for such breach are implemented in Article 5, except for Zero Tolerance Activities.

On the other hand, and perhaps just as obviously, cases may arise where the conduct of the Supplier to which the Buyer has not contributed is so egregious that immediate termination is required, with no opportunity for remediation, and this Article provides expressly for this as well. These cases involve what are called zero-tolerance activities in the EMCs.

The foregoing is elaborated in the following:

> (i) An Adverse Impact is not caused by a breach → Remediation Plan (Section 2.3) is required, if this Remediation Plan is not executed this results in a breach and triggers the remedies of Article 5
>
> (ii) An Adverse Impact is caused by a breach (for example, Supplier has not implemented or refuses to collaborate to implement proper Human Rights and Environmental Due Diligence and deploys irresponsible purchasing practices vis-à-vis subcontractors) → Remediation Plan is required and this may trigger the remedies of Article 5 (including termination and responsible exit)
>
> (iii) A breach has occurred but no Adverse Impact → The remedies of Article 5 are triggered (including termination and responsible exit)
>
> (iv) If a Remediation Plan fails not due to a breach by either Buyer or Supplier (for example regarding adverse impacts further down the supply chain) parties shall negotiate in order to find a solution to address the impact effectively. If they fail to reach an agreement the dispute resolution mechanism of Article 7 is triggered.

2. Section 2.1

It is important to note that the detailed summary as referred to in section 2.1 includes both the situation in which an Adverse Impact is imminent, and may still be prevented, as when it has occurred. The (joint) investigation set forth in section 2.2 regards both situations. The remainder of this article, sections 2.3-2.5, only govern the situation in which an Adverse Impact has occurred.

The phrase between brackets is intended to prevent a situation in which the obligation of Section 2.1 is triggered by very tiny environmental or human rights impacts. Such impacts should be dealt with by Supplier. It may be helpful to further define which impacts are material to Buyer in the specific circumstances.

3. Section 2.2

It is important to note that Article 7(4) of the CSDDD adopts the obligation for Buyers to bear the cost of third-party verification in relation to small and medium sized Suppliers.

4. Section 2.3

(a) The OECD Guidelines (as well as the UNGPs) concern those adverse impacts that are either caused or contributed to by the enterprise, or are directly linked to their operations, products, or services by a business relationship.[64] The OECD Guidelines further provide that an enterprise 'contributes to' an adverse impact or harm if its activities, in combination with the activities of other entities, cause the impact, or if the activities of the enterprise cause, facilitate, or encourage by incentives another entity to cause a harm and is not limited to minor or trivial contributions.[65] As stated there, the term 'business relationship' includes relationships with business partners,' including franchisees, licensees, joint ventures, investors, clients, contractors, customers, consultants,' advisers, entities in the supply chain, and 'other non-State or State entities directly linked to its business operations, products or services.'[66] The OECD Guidelines further provide that where a harm is directly linked to the operations, products, or services of a business, the business must use its leverage to influence the entity causing the harm to prevent or mitigate it.[67] Under UNGP 22 businesses are responsible for providing remediation where they caused human rights harm directly through their own operations and where they contributed to harm caused by others.

(c) Where Buyer fails to take reasonable action to address an Adverse Impact promptly after becoming aware of it, Buyer may be deemed to have contributed to any ongoing harm.

(d) It is important to note that remediation is both retrospective and prospective. It is retrospective because it attempts to make people whole for the harm they have suffered. It is prospective because it seeks to prevent recurrence. In this way, remediation is embedded within corporate sustainability due diligence. The forms of remediation in the clause are based on the commentary to UNGP 25.

64 See paragraphs A.11 and A.12 of the OECD Guidelines. See also OECD Due Diligence Guidance, at 20.
65 See OECD Due Diligence Guidance, at 23.
66 OECD Due Diligence Guidance, at 10 and 23.
67 OECD Due Diligence Guidance, at 24.

Article 8(3)(b) of the CSDDD requires such a remediation plan if the Adverse Impact cannot be immediately brought to an end. If an adverse impact cannot be brought to an end in an established business relationship. Recital 38 clarifies that companies should minimize the extent of such impacts, which requires an outcome which is the closest possible to bringing an adverse impact to an end. Recital 39 further elaborates this. The action to end or minimize the impact should be proportionate to the significance and scale of the adverse impact as well as the contribution of the companies conduct.

Under UNGP 24 businesses are entitled to prioritize and focus their attention on the most severe human rights harms or harms that become irremediable if there is a delayed response. A 'severe harm' is characterized by its gravity, the number of people that are or will potentially be affected, and the ability to make people whole. The severity of an Adverse Impact furthermore depends on the extent of the damage or potential damage to, or other effects on, the environment, the irreversibility of the impact and any limits on the ability to restore affected individuals or the environment to a situation equivalent to their situation prior to the impact. See also UNGP 14 defining in commentary what contributes to the severity of harm.

Cooperation among buyers who all purchase from the same troubled supplier can be especially effective, but buyers should keep in mind the European and member state competition laws. The European Commission currently prepares horizontal guidelines which provide guidance on the type of collaboration allowed between buyers to incentivize sustainability measures and, thus, also regarding such collaboration. Some member state competition authorities have done the same. In this regard Article 8(4) of the CSDDD as well as Recitals 35 and 35a include the option to conclude a contract with an indirect business partner in order to secure the implementation of a remediation plan. The contract should not preclude this based on competition law.

The OECD Due Diligence Guidance recommends remediation be risk based, prioritizing the most severe risks for corrective action.[68] In cases where it is not possible to bring to an end or mitigate all identified Adverse Impacts simultaneously, companies may prioritise the order in which they take appropriate measures. They should do so on the basis of the severity and likelihood of impacts and in a manner informed by meaningful engagement with affected stakeholders.[69] The company's degree of influence, leverage over or proximity to the subsidiaries or entities with which it has a business relationship should be considered to be less relevant to its prioritisation decisions.[70]

The appropriate remediation will depend on the nature and extent of the harm and the prioritization of risk. For example, many buyers choose to rate forced labor and child labor as high risk or Zero Tolerance.[71] Buyer may refuse Goods originating from a factory where such Zero Tolerance breaches have taken place and may require rigorous comprehensive remediation of that factory while maintaining the contract with other factories operated by Supplier when appropriate.

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[68] OECD Due Diligence Guidance, supra note 8, at 34–35, Annex Questions 41-45 and 48-54, accessible at http://mneguidelines.oecd.org/OECD-Due-Diligence-Guidance-for-Responsible-Business-Conduct.pdf.

[69] See also Recital 26a CSDDD.

[70] See the new paragraph 2a to Article 8 CSDDD proposed by the European Parliament, 2022/0051(COD), p. 77. See also Article 6a CSDDD.

[71] See Article 2.5.

Parties may contemplate to implement a dispute resolution option (including a binding escalation mechanism) with rights holders affected by the Adverse Impact in the remediation plan.

This section has been drafted broadly to provide Buyer and Supplier flexibility in crafting an appropriate industry-specific protocol for addressing Adverse Impacts by Supplier.

(e) The timeline to be implemented in the remediation plan depends on the type of Adverse Impact. The more severe or irreversible an impact is or the larger its scale, the faster it should be remediated.[72]

(f) Article 8(3)(b) of the CSDDD requires the development of a remediation plan (corrective action plan) in consultation with stakeholders.[73] Annex II to the Conflict Minerals Regulation[74] also includes an obligation to engage in a dialogue with the supplier, those impacted, local and national authorities and NGO's and to agree with those stakeholders on a plan to remediate this impact and to assess the effects of the plan in a measurable way, if a human rights impact is observed and the contract is not terminated or suspended.

(i) The term capacity building is found in the OECD glossary of statistical terms as the '[m]eans by which skills, experience, technical and management capacity are developed within an organizational structure (contractors, consultants or contracting agencies)—often through the provision of technical assistance, short or long term training, and specialist inputs (e.g., computer systems). The process may involve the development of human, material and financial resources.'[75]

5. Section 2.4

As is also elaborated in connection with Section 1.3(h), human rights remediation should not build on termination as current contractual mechanisms often do. Termination often worsens the human rights or environmental situation and is, generally speaking, in no one's interest.[76] The buyer does not want to suffer the disruption and incur the delay or switching costs to transfer its business to new suppliers. The supplier certainly does not want to lose business. And except in the most extreme circumstances, the workers do not want to lose their jobs and their livelihood. Therefore, this section requires remediating the problem commensurate with section 2.3 by taking measures to stop and correct the harm and to address any grievances. A right to cure is also essential to the ability of Supplier to avoid the human rights harms to workers and others that may result from the termination by Buyer of the Agreement.

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[72] Cf. the ruling of the Dispute Resolution Mechanism of the Dutch International Resonsible Business Conduct Agreement in the Textile Sector of 17 May 2021, para. 5.20 accessible at https://www.ser.nl/en/themes/irbc/-/media/FC631EE30DF7407583EF96608E14E49F.ashx and the ruling of 31 May 2022, para. 5.14 accessible at https://www.ser.nl/en/themes/irbc/-/media/A40B54F014DC4F3E9EAA36713487CCE7.ashx.

[73] See also Recital 26a CSDDD.

[74] Regulation EU 2017/821, https://publications.europa.eu/en/publication-detail/-/publication/8b0e378b-3c59-11e7-a08e-01aa75ed71a1/language-en/format-PDFA1A. This regulation is based on The *OECD due diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas*, accessible at https://www.oecd.org/corporate/mne/GuidanceEdition2.pdf.

[75] Glossary of Statistical Terms: Capacity Building, OECD, August 22, 2002, accessible at https://stats.oecd.org/glossary/detail.asp?id=5103.

[76] See also Recital 36a CSDDD.

Article 8(6) of the CSDDD and Recital 32 confirm that companies should continuously engage with their business relations and disengagement is a measure of last resort. Recital 36 also allows prioritizing engagement with business relationships in value chains instead of termination as a last-resort action after unsuccessfully attempting preventing and mitigating adverse impacts. If the adverse impact cannot be brought to an end Article 8(6) of the proposal and Recitals 36 and 41 also refer to the obligation to refrain from entering into new or extending existing relationships in such instance and, as far as allowed by the applicable law, suspend commercial relationships if it is expected to be successful on the short-term or terminate if the potential impact is severe. This section is also commensurate with Articles 7(5) and 8(5) of the CSDDD as these only allow termination if other due diligence measures by Buyer are not effective.

Furthermore, it only allows for termination of the Agreement if severe Adverse Impacts have not been cured or adequately mitigated in the cure period or cannot be cured, the Buyer has not contributed to the Adverse Impact and the Supplier has caused or contributed to the impact. Termination is not allowed if, for example, the Adverse Impact is observed further down the supply chain and is not caused or contributed to by the Supplier either. In such instances parties should negotiate in good faith to find a solution for the Adverse Impact. If they are unable to reach a solution this will trigger the dispute resolution mechanism of Article 7.

On should realize that remedy might be difficult to achieve and originally set timeframes might prove unrealistic, especially in relation to complex cases in which remedy has to be provided. The German Act therefore requires the remediation plan to consist of a timetable with different measures to be implemented and objectives to be achieved. Similarly, the CSDDD requires "reasonable and clearly defined timelines for action and qualitative and quantitative indicators for measuring improvement". Parties should also assess already achieved objectives and reassess timeframes. They should not terminate just because remedy they believed was possible until a certain moment in time takes longer to achieve.

6. Section 2.5

This clause attempts to balance the fact that certain violations of human rights are ultimately better addressed through the Remediation Plan process set forth above, as compared to other violations that cannot be tolerated even for an instant, the Zero Tolerance Activities. This is a difficult line to draw at times, and there is some divergence in practice and across legislation as to what may be tolerated and what is absolutely prohibited. One may limit this to severe Adverse Impacts (as Article 8 section 6(b) of the CSDDD does) or where the Buyer would be exposed to criminal prosecution. Where these lines are drawn and what may or may not be permissible are issues for each Buyer and Supplier to address based on applicable laws and policies. Note also the Supplier’s right to immediate termination without default under Article 1.3(g).

Practical Guidance to Article 2

1. Section 2.3

The responsibilities of Supplier and Buyer as set forth by Articles 2 and 5 in connection with Adverse Impacts and breaches of the agreement, as depicted in the scheme in the introduction of the general commentary may be further elaborated. For example, Buyer and Supplier should prepare a scheme regarding the required information (also regarding sub-suppliers if needed) and financial, technical and human recourses as well as on the division of cost of the measures connected to the Remediation Plan.[77]

Further practical guidance as how to divide cost between Buyer and Supplier as well as indicators to assess Buyer's contribution can be found in the BAFA Guidance.[78]

As the Remediation plan is primarily designed for rights holders (third parties to this Agreement), this raises the question whether any third-party rights to affected stakeholders should be granted in the Remediation Plan. Third-party beneficiaries are a controversial issue. One may either grant no such Third-Party Beneficiary rights, choose an in between solution or grant such rights.[79] Ideally, all adversely impacted stakeholders would be granted enforcement rights under this Agreement or more specifically in connection with a Remediation Plan, but there are significant commercial and practical obstacles to granting such third-party beneficiary rights.

Article 8(3)(g) CSDDD does not directly seem to require implementing such third-beneficiary rights in a supply chain contract. However and obviously, this article definitely allows for such a provision. Moreover, one should realize that Article 22 CSDDD provides access to remedies for affected rightsholders regardless of whether parties have granted such third-party rights in the agreement.

If parties wish to include such rights in a remediation plan (or more broadly), they may consider the language proposed in Corporate Accountability Lab.[80] It reads:

> 1.1. The Parties to this Agreement acknowledge and agree that the terms of this [Agreement][Remediation Plan][Schedule Q] are intended to benefit and protect not only the Parties but also persons directly impacted by (1) Supplier's and/or Buyer's activities performed under this [Agreement][Remediation Plan][Schedule Q] and (2) activities by subsuppliers that the Supplier contracts with to perform under this [Agreement][Remediation Plan]. Such persons include but are not limited to workers, landowners, property owners, those residing, working, and/or recreating in proximity to supply chain activities who are injured or suffer damages due

[77] Cf. BAFA Guidance ("Zusammenarbeit in der Lieferkette zwischen verpflichteten Unternehmen und ihren Zulieferern - Die wichtigsten Fragen und Antworten für KMU", 1ed June 2023), p. 4, 26, 29 and 30.
[78] BAFA Guidance ("Zusammenarbeit in der Lieferkette zwischen verpflichteten Unternehmen und ihren Zulieferern - Die wichtigsten Fragen und Antworten für KMU", 1ed June 2023), p. 30 and 31.
[79] The ultimate decision may be affected by the outcome of discussions with respect to a possible mandatory treaty on business and human rights. See The Third Revised Draft of a Treaty on Business and Human Rights by the Open-Ended Intergovernmental Working Group on Transnational Corporations and other Business Enterprises with respect to Human Rights (OEIGWG), established by U.N. Human Rights Council Resolution 26/9 (Aug. 6, 2020).
[80] See Towards Operationalizing Human Rights and Environmental Protection in Supply Chains: Worker-Enforceable Codes of Conduct, February 2021, https://static1.squarespace.com/static/5810dda3e3df28ce37b58357/t/6026fd326aa9cd4f88697a20/1613167923256/Towards+%20Operationalizing+Human+Rights+and+Environmental+Protection+in+Supply+Chains.pdf.

to Adverse Impacts [breach of Schedule Q], including survivors of those killed or disabled. Such persons are intended thirdparty beneficiaries to this [Agreement][Remediation Plan][Schedule Q].

1.2. All intended third-party beneficiaries of this [Agreement][Remediation Plan][Schedule Q] have the right to enforce this [Agreement][Remediation Plan][Schedule Q] against Parties in any court or tribunal that has jurisdiction over the [Buyer/Supplier or Agreement/Remediation Plan/Schedule Q].

1.3. Third-party beneficiaries may assign their rights to a labor union, nongovernmental organization, or other organizations providing legal assistance they select.

If this language is adopted it is necessary to consider its relation to other dispute resolution mechanisms and parties should note in particular Article 7. For example, it may be helpful to implement a system of dialogue-based dispute resolution with rightsholders paired with an escalation mechanism if the dialogue fails (either in national courts or through arbitration) as envisaged by Article 7 in the relation between Buyer and Supplier. That said, recourse to existing dispute resolution mechanisms, such as the International Accord in the Garment Sector, the ACT mechanism and National Contact points of the OECD, may be an option too. In case such existing mechanisms are deployed parties should decide how, and implement language on, the decisions of these mechanisms should be dealt with in view of their contractual obligations.

An example of an in between solution is the following. Two alternatives are given here. When licensing is involved, those parties choosing the first bracketed option will want to consider giving enforcement rights to licensors and/or licensees and not only Buyers and Suppliers:

> All buyers and suppliers in the supply chain have the right to enforce the relevant provisions relating to the human rights protections set forth herein [and in Schedule Q] and privity of contract is hereby waived as a defense by Buyer and Supplier provided, however, that there are otherwise no third-party beneficiaries to this Agreement. Individuals or entities, including but not limited to associations, workers, land owners, property owners, those residing, working and/or recreating in proximity to supply chain activities and any individual who is injured or suffers damages due to an Adverse Impact have no rights, claims, causes of action or entitlements against Buyer or Supplier arising out of or relating to this Agreement, [Schedule Q] or any provision hereunder[, unless such rights are expressly stipulated regarding specific individuals or entities in the Remediation Plan in connection with the implementation of the Remediation Plan]. The parties agree that no consent from the individuals or entities referred to in this section is required for Buyer and Seller to vary or terminate this Agreement (whether or not in a way that varies or extinguishes rights or benefits in favour of such individuals or entities).]

If a third-party beneficiary clause is implemented one should note that Article 1200 of the French Code Civil rules that contractual rights may only be exercised between parties. Therefore, third-beneficiary rights are challenging. That said, these third parties may have a tort claim against the Buyer or the Supplier based on the Adverse Impact. Under Italian law, a contract in favor of a third party grants such third party the right to receive performance from one or more of the contracting

parties; such stipulation in favor of a third party is valid if the contracting party has an interest in it. The third party never becomes a party to the contract, although it is entitled to obtain performance. Under English law, the parties can choose who the third-party beneficiaries are. It should be noted that the list of intended third party beneficiaries is very broad compared to those one might ordinarily see (which is usually limited to specific parties who may have an interest in the transaction, such as group companies of one or more of the contracting parties), and that therefore the Buyer could be exposed to a proliferation of actions. In some cases, where the proposed third parties are very removed, it is not clear what the mechanics would be for them to enforce the contract in practice.

As an aside, it should be noted that a very unusual aspect of English law is that if third party beneficiaries are included, wording stating that the agreement can be amended/terminated without the consent of third-party beneficiaries should also be included, otherwise such consent is required for any such amendment/termination to be effective. An example of such wording is as follows: '*The parties agree that no consent from the persons referred to in [the third-party rights clause] is required for the parties to vary or rescind this Agreement (whether or not in a way that varies or extinguishes rights or benefits in favor of such third parties)*.'
Article IV.A-2:305 of the Draft Common Frame of Reference includes a provision on third party rights and will allow a providing for these rights.

2. Section 2.4

The former Bangladesh Accord (currently International Accord) provides some additional guidance on responsible exit.[81] It includes three stages. First a letter should be sent to the supplier management to inform it, it is in breach of the remediation plan and to give a specified number of days to bring about specified improvements, if these are implemented no further steps are necessary. If not, the management of all the brands sourcing from the factory send a warning letter to the supplier, stating that if the steps specified in the remediation plan are not taken within a specified number of days these brands are legally required to terminate the relationship. At this point the Accord Secretariat, the supplier and the brands to explain how disengagement should proceed, if necessary, and to determine whether additional financial commitment from the brands is required. The third step is responsible disengagement if the requirements of the remediation plan are not met within the specified time. This implies collective disengagement by all Accord brands. However, the brands are still responsible for compensating workers for termination of work resulting from disengagement, but no longer for other cost. This implies, for example, that the disengaging brands are expected to temporarily pay workers' salaries, and the brands have to make reasonable efforts to find alternative employment for the workers as the working environment is unsafe in such cases. This is especially important for union leaders who may have pointed at the issue and may be blacklisted. Blacklisting results in difficulty in finding future work. In such cases the Accord may also intervene. The supplier then remains blacklisted for 24 months and may reapply after that. That said, in case of acute fire or building danger the escalation protocol may be skipped and a buyer may immediately move to disengagement. This is an interesting example as it uses

[81] The Bangladesh Accord 'escalation protocol' for responsible engagement and disengagement. See on this OECD Watch, Legislating due diligence: Respecting rights or ticking boxes?, p. 26, accessible at https://www.somo.nl/respecting-rights-or-ticking-boxes/.

collective leverage of buyers sourcing from a specific facility to increase the credibility and eloquence of the threat of disengagement, which is a more powerful instrument than such a threat expressed by a single buyer. This is not a feature which as such can be included in model supply chain contracts, but it can be part of multi-stakeholder initiatives and collaboration between buyers to increase leverage. It should also be noted that disengagement does not terminate responsibilities of the buyer towards workers, especially regarding their compensation and, if applicable, reasonable efforts to find alternative employment for them. Beyond this, a model contract may include a provision stipulating that the buyer will not reengage with the supplier during a specified period of time, for example, 24 months. This also increases the threat of disengagement. It is to be expected that European multi-stakeholder initiatives, such as the Dutch International Responsible Conduct Agreements and the Fair Wear Foundation, may consider and implement this disengagement approach as a best practice.

Member State specific comments to Article 2, UK and DCFR

1. France

2. Germany

In a supply chain where a supplier typically has a low number of buyers, the information right in Art. 2.1 a) might be feasible. However, where suppliers have many buyers, this creates a big bureaucratic burden as the supplier would have to invest a lot of time in communicating the same violation to many buyers. That might also lead to problems under German contract law (unreasonable T&Cs can be voided under Sec. 307 of the German Civil Code). In cases of smaller violations, suppliers might also be able to handle them alone and quickly (e.g. small breaches of workplace protection rules). Therefore it might generally or at least in the described situations be more recommendable to restrict this information obligation for individual cases to severe violations and otherwise only require summaries, for example on a yearly basis.

Section 2.2 and 2.3: Under the new Guidance of Helpdesk & BAFA (Executive Summary Collaboration in the Supply Chain, 1st ed June 2023, p. 5), buyers are generally obliged to participate in the costs of preventive and remedial measures according to the adequacy criteria - i.e., it might be that suppliers or buyers have to share the costs, esp. depending on the contributions to violations that are found and according to capacity of each. Relieving SMEs of costs for investigations is generally in line with that, but an addition referring to the adequacy criteria would be helpful. It might be a good idea to let suppliers pay where violations are found that the buyer did not contribute to. The same reasoning should apply for remediation plans.

Third-party rights are not addressed by the EMC, but might be in need of addressing. As to the EMC choice of leaving the issue of third-party rights untouched, this should be possible under German law. According to § 328 (2), the absence of any specific agreement by the party would leave it to the courts to interpret the intention of the parties in the light of the circumstances and the contractual purpose. Given that the EMC have the purpose of protecting others than the contracting parties, it is possible that a court would agree that third-party rights derive from the contract. German law also contains another, quite specific, version of third party rights: The contract with protective effect vis-à-vis third parties (Vertrag mit Schutzwirkung zugunsten Dritther). This category has been developed by the courts in analogy to the rules on contract with third party rights. The contract with protective effect vis-à-vis third parties is a category that creates protective duties towards a narrow group of protected third parties that are related to the contract, where one of the parties has an interest in including the third party (because of an obligation to protect), where inclusion is foreseeable for the contracting parties and the third party is in need of protection. Claims based on a contract with protective effect only cover breaches of protective duties and thus are more akin to tort claims than to contract claims. To consciously design this issue and not leave it to deciding courts, third party rights could be explicitly excluded or explicitly included. In fact, while under German law, it is also possible for third parties suffering from non-compliance with EMC to file a claim under tort law (§ 823 BGB), the narrowness of German tort law (in requiring breach of one of the enumerated rights, default and negligence) makes this rather difficult. The contract with protective effect vis-à-vis third parties is a possible contractual solution. Finally, regardless of whether the clauses create or not

create third party rights, German law always requires determining precisely what contractual obligations (in the interest of third party or protecting a third party) has been breached. Hence, the debate on third party rights is strongly connected to the debate on obligations under EMC, Art. 1 and the question on one-sided or shared responsibility.

As to the option of excluding third party rights: In general, German contract law starts from the premise of an autonomy of the contracting parties to determine the contract (§§ 116, 145 BGB). Consequently, parties are also able to specifically agree on whether they want a third party to be part of the contract. In addition, § 328 BGB contains an explicit provision on the possibility of third-party rights and equally declares the stated intention of the parties to be relevant. Based on these rules, there would not be a problem with either clauses, i.e. excluding or creating third party rights. However, there are also positions in the academic debate suggesting that exclusion of third party rights would be problematic either because such would be contrary to the essential obligations under the law on unfair contract terms control (which is ensuring human rights respect and thus creating a position for rightsholders) or because of general contract law principles (in particular the prohibition of contradictory behaviour, venire contra factum proprium). There is not yet any case law on third-party rights for contractual clauses that relate to human rights respect and thus no indication on what the case law will suggest. Regardless of the agreement of the contract,

Additionally attention should be given to the implications under the German Supply Chain Act and CSDDD – these might argue for explicitly including third party rights: The German Supply Chain law can be read (there is legal debate on this and a lack of certainty, but the better arguments argue for an inclusion) and the CSDDD clearly needs to be read as including an obligation to effectively repair victims violated in their environmental or human rights by breaches of environmental or human rights due diligence. And both include obligations on providing potential and actual victims access to remedial mechanisms, which have to be accessible for employees and others at the supplier level and in the supply chain. Thus, if a violation is determined under the procedures under such mechanisms, repair for the victims would need to follow. This would include victims at the supplier level and in these cases likely mean that buyer and supplier will adequately share the costs according to contributions/capacity, likely with a special onus on the supplier since the violations will be likely to derive from his sphere and actions. In such a situation, this clause might be used by the supplier to deny participation in the remediation, as this would imply a benefit for a third party which is by this clauses explicitly included. Under German Civil Law, a lack of security of interpretation of T&Cs can be used against the creator/user of the standard clause, which would likely be the buyer, Sec. 305 c (2). Therefore, this clause might hinder the effective collaboration between buyer and supplier and remedy and create the risk that the buyer will face the arising costs alone. Under the CSDDD, Article 22 creates a civil liability provision for third parties against obliged buyers anyway, making the exclusion of contractual third party rights futile. An exclusion of this clause is therefore recommended and a clear allocation of responsibilities between buyer and supplier in the case of third party victims to be preferred.

Section 2.4 and 2.5: This clause complies with German law's general priorisation of performance and the right to cure over termination and rescission. It is to be noted, however, that considerable improvements that are achieved or can be expected are enough for an exit not to be required under LkSG, see Sec. 7 (3) No. 2 with Sec. 7 (1), s.1 - a "minimization" of a violation is also considered a

remediation. Exceptions from the requirement to set a notice period exist (among others) in case Supplier refuses performance seriously and definitively, and if special circumstances, having weighed the interests of both parties against each other, justify immediate termination. This would be the case both if the Remediation Plan fails and Supplier has engaged in a zero tolerance activity. German law however only allows for termination within a reasonable time period after gaining knowledge of the reasons for termination (section 314 § 3 German Civil Code). This provision intends to force the parties to create clear relations as early as possible. Under German law on general terms and conditions, clauses providing for rights to terminate or rescind in case of any violation are ineffective.

3. Italy

Sections 2.1 and 2.3: With respect to any contractual claim that Buyer might wish to raise following an alleged Schedule P violation, it must be pointed out that, under Italian law, it is not possible to assess *ex ante* whether the procedure outlined in Section 2.1 would *per se* generate the documentation and evidence necessary for the enforcement of the contractual obligations allegedly breached by the Supplier or to deal with enforcement authorities. This assessment should be made on a case-by-case basis, considering the content of the notice, attachments (if any), and the specific circumstances of the case.

Beyond this, and unless specifically approved in writing by means of a double signature *(doppia sottoscrizione*), the general terms that establish, in favor of the party which unilaterally drafted them, limitations of liability, the right to withdraw from the contract or suspend its execution or provide for the other party the penalty of forfeiting rights, limitations on the right to oppose exceptions, restrictions on contractual freedom in dealings with third parties, tacit extension or renewal of the contract, arbitration clauses or exceptions to the jurisdiction of the judicial authority, are not valid under Italian law.

Section 2.3(d): Under Italian law, requiring Supplier to terminate an agreement or affiliation with a specific factory, terminate a subcontract or remove an employee or employees and/or other Representatives may potentially (if coupled with other undue influences on the Supplier's activities) fall within the scope of the Italian rules on the abuse of the economic dependence and/or "direction and coordination" activities (respectively, under article 9 of Law no. 192/1998 concerning the "Regulation of subcontracting in productive activities" and article 2497 and ss. of the Italian Civil Code) to the extent the exercise of such rights is excessive or not adequately justified by factual circumstances and material breaches by Supplier. Therefore, validity and implications of this provision will primarily depend on factual circumstances and on the way in which it is actually enforced. In case the rules on abuse of economic dependence are breached, the agreement through which the abuse of economic dependence is exercised is to be considered null and void and actions for injunctions and damages may be brought by the affected party. If, instead, the rules on 'direction and coordination' activities are triggered, leaving aside certain additional disclosure obligations, provided that certain additional requirements are met, Supplier might be held liable for the damages it has caused as a consequence of the abuse of the 'direction and coordination' activities.

Section 2.5: With reference to the Italian legal system, the definition of 'Zero Tolerance Activity' may be supplemented with the reference to the activities or omissions which may result in liability pursuant to Italian legislative decree of June 8, 2001, no. 231.[82]

4. Poland

Section 2.2: Polish law protects the party in breach's 'right to cure' but parties are free to define 'incurable' breaches in a contract warranting immediate termination.

Section 2.3: Polish law does not include the principle of 'certainty of terms' sensu stricto. Nevertheless, terms which lack certainty can be difficult to enforce, found void or affect the validity of the entire contract under the principle of 'essentialia negoti' according to which essential terms of a contract must be sufficiently specified.

The provisions concerning the 'Remediation Plan' and its inclusion as a binding part of the parties' contract, may pose challenges under the discussed principles because of the uncertainty of the obligations stemming thereof.

A requirement for the Supplier/Buyer to submit to an accessible procedure for resolution of disputes with the affected stakeholders and to conduct such disputes constructively, may be more operable.

A procedure in which the Remediation Plan will be drawn up by an impartial expert adjudicator, whose decision may be accepted by the Parties or not, or in which it will be set in a binding manner by an arbiter authorized to decide the matter ex equo et bono, could be considered.

In any case, elaboration of some objective parameters which should govern the drafting of the Remediation Plan and the distribution of the burdens connected with its implementation, is desirable, if the obligation to prepare and implement it is to be legally binding and not merely 'relational'.

5. Portugal

6. Spain

Section 2.1: Under Spanish law there are no formal requirements for general notices of breach. However, in order to avoid a potential challenge regarding the validity and veracity of the notice in a potential future claim, it would be advisable to deliver such notices by a means that allows for the certification of its receipt and content (e.g., burofax, notarial requirement, etc.)

Sections 2.2 and 2.3: according to article 1.102 of the Spanish Civil Code, any limitation of liability (either as regards the amount or the capacity to claim it) is not enforceable when the party who claims the limitation acted with wilful intent ("*dolo*"). Therefore, in the event of wilful misconduct of the Supplier, a judge may consider that the Client is not obliged to follow the order of remedies

[82] This decree governs the administrative liability of corporations for criminal conducts of their representatives and includes a list of underlying offenses that trigger such liability.

established in the agreement (i.e., Investigation and Remediation Plan) and shall be entitled to directly claim the losses suffered.

Clause 2.5: Although, the Spanish Civil Code recognizes the right to terminate for fear of breach ("*fundado temor*") in some specific cases (arts. 1502, 1503, 1467 CC), these rules cannot be applied analogically to any situation. In general terms, under Spanish law and in accordance with courts past practice, to terminate an agreement for breach, there should be sufficient satisfactory evidence that a breach has occurred (termination for potential breach is not accepted under Spanish law). Since Spanish courts have embedded the principle of conservation of agreements, a breach should be material and effective to result in termination of the agreement.

7. UK

Section 2.1: There are no formal requirements for notice of breach under English law. It is to be expected that in the ordinary course of business written materials and records will be generated in relation to Supplier's performance, but it is not usual to include details of these in the contract. It is also expected that the confidentiality clause permits disclosure to regulators if required.

Section 2.3: The inclusion of this process around a remediation plan does not affect the parties' rights under English law, save that the Buyer will need to wait for the parties to go through these extra procedural steps around the remediation plan before terminating the Agreement for non-compliance, unless the Supplier has engaged in a Zero Tolerance Activity. Although the concept of a remediation plan aligns with expectations under soft law standards and the approach seen in other contexts (e.g. project financings under the Equator Principles), difficulties are envisaged in practice with characterizing such plans as tools to restore affected stakeholders to the situation they would have been in had the adverse impact(s) not occurred given the complexity and nature of human rights issues. Section 2.3(b) may be especially challenging in this regard. An alternative could be to include a requirement that the Supplier obtain the Buyer's approval (or the approval of an appointed technical consultant) in preparation of the plan.

8. Draft Common Frame of Reference (DCFR)

Section 2.3(d) is commensurate with Article III-401 DCFR. Sections 2.4 and 2.5: Articles III-3:202 and III-3:204 DCFR include a right to cure and govern the consequences of it. That said, Article III-3:203 allows termination without the right to cure under certain conditions. Parties may further negotiate such conditions as is set forth by section 2.5.

However, section 2.4 may be suspect under Article III-3:105(2) if non-termination would violate good faith and fair dealing. However, it is expected that this would rarely happen. It may also be contrary to Article III-3:502 if the non-performance is fundamental, which may be the case regarding human rights violations. However, one may argue this section is connected with providing the supplier a period of time to cure the non-performance which is allowed under Article III-3:202.

Article 3 Rejection of Goods

3.1 Rejection of Nonconforming Goods

In the event of a severe Adverse Impact that Supplier has caused or to which Supplier has contributed that renders the Goods Nonconforming Goods, Buyer shall have the right to reject them unless Buyer's breach of its obligations under Section 1.3 [and/or Schedule Q] materially caused or contributed to the Adverse Impact. Goods are Nonconforming Goods if the goods cannot pass without objection in trade or if the Goods are associated with a Zero Tolerance Activity. Article 1.3 (h) applies to this rejection.

3.2 Timely Notice

Notwithstanding any provision of this Agreement or applicable law (including without limitation [the Inspection Period in Section ____ of this Agreement and]), Buyer's rejection of any Goods as a result of an Adverse Impact shall be deemed timely if Buyer gives notice to Supplier within [8 days] [period agreed by parties] [a reasonable time] after Buyer's discovery of same, and, in any case, to the extent such discovery is communicated within one year from the delivery of the Nonconforming Goods.

General commentary to Article 3

1. Introduction

This section is important as goods tainted by human rights violations, for example connected to forced labor, may not pass without objection in trade.[83] This is especially relevant where seizure of goods by customs is impending or as actually happened. This may be the consequence if goods are produced with forced labor according to Articles 6, 17 and 19 of the previously mentioned Draft Regulation on Forced Labor.

2. Section 3.1

Nonconforming Goods are presumably defined elsewhere in the supply chain contract, for example, with respect to conformity to product specifications. This section clarifies that goods that conform to product specifications may nevertheless be rejected in the circumstances specified in the text. Note that this requires causing of or contribution to an Adverse Impact by Supplier. This is not necessarily the case if this impact occurs further down the supply chain. In such instances it may be conceivable that Supplier has undertaken proper due diligence as defined in Article 1.1 but the Adverse Impact nevertheless occurs. Then the remedy implemented in Article 3.1 will not be available to the Buyer. This may be relevant because the risk of seizure of goods tainted by human rights abuse as explained in the introduction. If the goods cannot be released into the Union market or otherwise sold where and when Buyer intended, Buyer must have the right to reject the Goods as Nonconforming Goods. Similarly, if Buyer cannot sell the goods in the ordinary course of business, it should have the right to reject the Goods unless Buyer's own actions caused or contributed to the problem in a material way.

If the Supplier is a small or medium sized enterprise, Article 7(4) of the CSDDD requires that the contractual assurances obtained shall be fair, reasonable and non-discriminatory. It should be considered whether rejection of goods will be considered as such in all circumstances.

3. Section 3.2

Articles 38–40 of the CISG require that Buyer examine the goods or cause them to be examined within as short a period as is practicable. Buyer loses the right to rely on a lack of conformity if Buyer does not give Supplier notice within a reasonable time after Buyer discovers or ought to have discovered a defect and, at the latest, within two years of the date of delivery (or other contractual period) unless Supplier knew or could not have been unaware of the defect. Contract law of most member states include such limitations and usually mention a reasonable time after the discovery of the defect.

The terms 'Nonconforming Goods' and 'Inspection Period' are assumed to be defined earlier in the supply chain agreement. Nevertheless, Nonconforming Goods are defined specifically for purposes related to human rights policies in Section 3.2.

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[83] See for example Article 3 of the proposed Regulation of the European Parliament and the Council on prohibiting products made with forced labour on the Union Market, Com(2022) 453 final, accessible at https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52022PC0453&from=EN.

Practical guidance to Article 3

Member State specific comments to Article 3, UK and DCFR

1. France

Section 3.4: Article 1218 Code Civil includes a reasonable period after discovery of the defect in which a contractual party must inform the other party of the defect.

2. Germany

The model clauses provide for several termination rights, amongst others in this article and in Articles 1.3, 2.4 and 2.5. Implementing such a right in different places creates a risk of the contract not being clear, and thus, of being void under German law governing general terms and conditions. The requirements on termination rights (right to cure, responsible exit) and on adequate addressing of violations with preventive and remedial measures would most likely also apply to the clauses 3.1-3.3 as they effectively make it possible to at least partially terminate the contract. It would therefore be recommended to either include the corresponding requirements in them as well, strike this clause out altogether or simply include the option of rejecting goods in Sec. 2.4 and 2.5 as an option before termination. This would also be in line with the recommendation under the LkSG to take into account the temporary suspension of a contract in cases of breach, see Sec. 7 (2) No. 3. Additionally, the notion of "goods cannot pass without objection in trade or if the Goods are associated with a Zero Tolerance Activity" is problematic as it is not restricted to any tier of the supply chain of the good and as it is very open - i.e., the buyer effectively shifts the risk of violations occuring in the deeper supply chain to the supplier. Such violations might, depending on the industry, be very widespread and hard to avoid, but only possible to improve step by step, with buyer and supplier working collaboratively. Making the supplier, esp. if it is a SME, solely liable for such situations therefore risks violating the requirements on sharing responsibility according to capacity and contributions under Helpdesk & BAFA Guidance, the requirements under CSDDD to have proportionate clauses for SMEs and German Civil Law on reasonable and well defined terms and conditions (Sec. 305 and 307 German Civil Code).

3. Italy

One should note that Article 1495 of the Italian Civil Code requires a buyer to notify defects within 8 days of their discovery of within the different term agreed upon by the parties and, in any event, within 1 year of delivery of the goods.

4. Poland

Under Polish law rejection of non-conforming goods is tantamount to avoidance of the contract. The contract is then considered void *ex tunc* and performances must be returned. However, it is allowed under the principle of freedom of contracts to negotiate the consequences of the goods being non-conforming in the way stipulated in the model clauses (provided that it does not provide the Buyer with the opportunity to deny payment to the Supplier at the Buyer's undue discretion). That said, It would probably be more suitable under Polish law to draft the currently envisaged remedies concerning the non-conforming goods as part of the agreed 'mitigation of loss procedure' – which means to leave it at the Buyer's discretion whether to reject the goods in the strict sense and return them for reimbursement of the price (which right should be limited by a fixed reasonable deadline)

or to keep them but dispose of them appropriately in an effort to mitigate the loss caused by their non-conformity, and to claim appropriate damages from the Supplier afterwards.

5. Portugal

6. Spain

Pursuant to article 1255 of the Spanish Civil Code, which establishes freedom of contract, article 3 would be enforceable under Spanish law, although it would be advisable that it is clarified in more detail which Adverse Impacts would turn the Goods into Nonconforming Goods.

7. UK

Section 3.1: this section provides for an obligation on the Buyer, Supplier and Representatives to engage in human rights due diligence (in accordance with sections 1.1 and 1.2) so as to ensure compliance with Schedule P. It may well prove challenging to obtain an order requiring a party to comply with certain positive contractual obligations of this nature.[84] That said, Article 3 also provides for certain express rights to reject nonconforming goods; and to terminate the contract in the event of certain breaches. These contractual remedies mean that the issues identified with the other remedies may be less important.

8. Draft Common Frame of Reference (DCFR)

Section 3.3: Article III-3:103 DCFR includes a notice as required by this section. A failure to notify the other party of a defect within reasonable time may also restrict remedies under Article III-3:107 DCFR. Article IV.A-2:308 DCFR includes a more specific rule regarding sales contracts.

[84] See also the comments on UK law regarding section 6.2(b).

Article 4 Nonvariation of Matters Related to Adverse Impacts

4.1 Course of Performance, Established Practices, and Customs

Course of performance and course of dealing (including, without limitation, any failure by Buyer to effectively exercise any audit rights) shall not be construed as a waiver and shall not be a factor in Buyer's right to reject Nonconforming Goods, terminate this Agreement, or exercise any other remedy. Supplier acknowledges that with respect to Adverse Impacts, any reliance by Supplier on course of performance, course of dealing, or similar conduct would be unreasonable. Supplier acknowledges the fundamental importance to Buyer of the prevention and/or mitigation of Adverse Impacts and understands that no usage or practice established between the parties should be understood otherwise, and any apparent conduct or statement to the contrary should not be relied upon. [Buyer acknowledges the fundamental importance to Supplier of the matters in Schedule Q and understands.] Parties understand that no usage or practice established between them should be understood otherwise, and any apparent conduct or statement to the contrary should not be relied upon.

4.2 No Waiver of Remedy

Buyer's acceptance of any Goods in whole or in part will not be deemed a waiver of any right or remedy nor will it otherwise limit Supplier's obligations, including, without limitation, those obligations with respect to indemnification.

General commentary to Article 4

1. Introduction

This article prevents that course of performance, course of dealing or failure to exercise rights may be considered as a waiver of rights.

Section 4.1

The last phrase of this section uses the terminology of CISG Article 9(1).

One may note that the language between brackets is mainly relevant in supply chains in which Buyer has leverage and is able to 'dictate' the conditions of the Agreement. If such leverage lacks, this language may not be relevant.

Member State specific comments to Article 4, UK and DCFR

1. France

2. Germany

This clause might be a derogation of § 377 German Commercial Code, if the issues covered would be interpreted as a defect in the terms of that provision. This could be disputed, since the provision primarily addresses material defects. If it would be considered a derogation, this derogation could be considered an unreasonable disadvantage under § 307 German Civil Code.

3. Italy

4. Poland

Limits on interpretation/modification by conduct will be valid and enforceable as long as they are not used to endorse an unconscionable, inconsistent conduct.

Section 4.1: this section provides for no informal modification in the matters concerned. This section may well serve as 'lex specialis' to any modification rules in the supply chain agreement, which may be more liberal and therefore inappropriate here.

5. Portugal

6. Spain

Article 1258 of the Spanish Civil Code states that agreements once executed create binding obligations for the parties not only in relation to the terms expressly included therein but also to all consequences that result from good faith. Therefore, although a waiver of course of performance and course of dealing is valid under the principle of freedom of contract, if the Client had knowledge of a situation which could lead to termination for a long period of time and has not taken any action in its respect, it could be considered that the Buyer has created a lawful expectation for the Supplier that such situation would be accepted and, therefore, termination of the agreement for such reason could be considered in bad faith.

7. UK

8. Draft Common Frame of Reference (DCFR)

Article 5 Remedies

5.1 Breach and Notice of Breach

(a) Both parties may be in the position of an aggrieved party and a defaulting party if both parties caused or contributed to a breach of due diligence obligations set forth by Article 1 or a failure to establish or implement a Remediation plan in accordance with Article 2.3, in which case each party has the rights and duties of both an aggrieved party and a defaulting party.

(b) Upon becoming aware of a breach of due diligence obligations set forth by Article 1 or a failure to establish or implement a Remediation plan in accordance with Article 2.3 Human Rights and Environmental Due Diligence("Default"), the aggrieved party shall promptly notify the other party of the following matters:

(i) that the party has formed the view that a Default has occurred and the party's reasons for that view;
(ii) reasonable details of the breach;
(iii) that the defaulting party must prepare and implement a corrective action plan (the "Corrective Action Plan") in accordance with this clause.

(c) Upon receiving notice, the defaulting party shall prepare, and submit to the other party within [___] days, or such other timeframe as agreed, a Corrective Action Plan that includes:

(i) the steps that the defaulting party proposes to take (the "Corrective Steps") to cure the breach;

(ii) a timeline for the completion of the Corrective Steps, to be agreed between the parties;

(iii) an explanation as to how the Corrective Steps will correct the Default; and

(iv) quantitative and/or qualitative indicators for determining when the Corrective Steps are completed.

(d) The defaulting party shall take all reasonable steps to implement the Corrective Action Plan within the timeframe agreed and provide to the aggrieved party reasonable evidence of the implementation of the Corrective Action Plan.

(e) The aggrieved party shall provide reasonable assistance to the defaulting party in preparing and implementing the Corrective Action Plan. Assistance may include, to the extent reasonable, in-kind contributions, capacity-building, and technical or financial assistance. If the aggrieved party has caused or contributed to the breach related to not implementing or not undertaking Human Rights and Environmental Due Diligence, it shall provide such assistance in amounts that are at least proportionate to its own contribution.

(f) In the event of a breach related to not implementing or not undertaking Human Rights and Environmental Due Diligence that is attributable to a factory or company designated by Buyer or an employee of Buyer, Buyer shall be responsible for ensuring that the designee cures this breach. If cure is not reasonably possible within an appropriate timeframe or is not accomplished in the timeframe set by Buyer, Supplier shall have the right to require that it is granted the right to source from another supplier. Article 1.2 and 1.3 (h) applies to this termination and consecutive sourcing.

(g) A failure by the defaulting party to prepare, or properly implement, a Corrective Action Plan is a material breach of this Agreement, and the aggrieved party shall have the right to exercise its remedies under Section 5.2.

5.2 Exercise of Remedies

(a) Remedies shall be cumulative. Remedies shall not be exclusive of, and shall be without prejudice to, any other remedies provided hereunder or at law. A party's exercise of remedies and the timing thereof shall not be construed in any circumstance as constituting a waiver of its rights under this Agreement. This party's remedies include, without limitation:

(i) Demanding adequate assurances from the other party of due performance in conformity with this Agreement. Such assurances shall be fair, reasonable and non-discriminatory.

(ii) Obtaining specific performance and/or interim measures, such as but not limited to injunctive relief with respect to a party's noncompliance with the obligations mentioned in section 5.1.

(iii) Suspending payments, whether under this Agreement or other agreements, until a party determines, in this party's reasonable discretion, that the party in breach has taken appropriate remedial action following the expiration of the cure period indicated in Section 2.3(d)(iv).

(iv) Terminating this Agreement if permitted by Sections 2.4(b), 2.5, or 3.3 and in accordance with Article 1.3(h) on responsible exit.

(v) Obtaining damages caused by the breach; provided, however, that if Buyer's breach of Section 1.3 [and/or Schedule Q] caused or contributed to the Adverse Impact, damages shall be reduced according to the contribution of Buyer to this Adverse Impact.

(vi) If a party has reasonable grounds for insecurity with respect to the other party's performance of this Agreement, this party may demand adequate assurances that the other party will perform. This party may suspend its performance until adequate assurances are received. If adequate assurances are not received in a reasonable time, the other party has breached, and this party may terminate this Agreement.

5.3 Damages

Buyer and Supplier acknowledge:

(a) Neither Buyer nor Supplier should benefit from an Adverse Impact occurring in relation to this Agreement. If damages are owed that would result in a benefit to Buyer or Supplier, such amounts should go toward supporting the remediation processes set out in Section 1.4 and Article 2. A "benefit" is here understood to mean being put in a better position than if this Agreement had been performed without an Adverse Impact. Nothing herein limits the right of a party to be put in the position it would have been in had this Agreement been performed without an Adverse Impact.

(b) [If there are insufficient funds to pay damages and complete the remediation processes set out in Section 1.4 and Article 2, remediation shall take priority.]

5.4 Return, Destruction or Donation of Goods; Nonacceptance of Goods

(a) Buyer may, in its sole discretion and if permitted under applicable law, destroy or donate the Nonconforming Goods, except to the extent that Buyer has caused or contributed to the nonconformity by breach of Section 1.3 [and/or Schedule Q]. Article 1.3 (h) applies.

(b) Buyer is under no duty to resell any Nonconforming Goods produced by or associated with Supplier or its Representative who Buyer has reasonable grounds to believe that Supplier has not implemented or undertaken Human Rights and Environmental Due Diligence in compliance with Article 1.1 or has not established or executed a Remediation Plan in accordance with Article 2.3, whether or not such noncompliance was involved in the production of the specific Nonconforming Goods. Buyer is entitled to discard, destroy, export or donate any such Nonconforming Goods. Notwithstanding anything contained herein to the contrary or instructions otherwise provided by Supplier, destruction or donation of Nonconforming Goods rejected, and any conduct by Buyer required by law that would otherwise constitute acceptance, shall not be deemed acceptance and will not trigger a duty to pay for such Nonconforming Goods. Buyer and Supplier agree that this Section and any related Sections are an effort to mitigate damages, as selling, profiting from, and being associated with tainted goods or Nonconforming Goods is likely to be damaging to Buyer, including to Buyer's reputation.

(c) If, in default of this Agreement, Buyer fails to accept and/or pay for goods that conform to this Agreement, Supplier may store them or resell them and will be made whole by Buyer through damages. Supplier will not resell goods made in material violation of the human rights or environmental standards stated in this Agreement; such goods shall be donated to charity.

5.5 Indemnification; comparative fault calculation

A party shall, in case of a breach of this Agreement, indemnify, defend and hold harmless the other party and its officers, directors, employees, agents, affiliates, successors and assigns (collectively, "Indemnified Party") against any and all losses, damages, liabilities, deficiencies, claims, actions, judgments, settlements, interest, penalties, fines, costs or expenses of whatever kind, including, without limitation, the cost of storage, return, export or destruction of Goods, reasonable attorneys' fees, audit fees that would not have been incurred but for the breach, the costs of enforcing any right under this Agreement or applicable law, in each case, that arise out of the breach, and if applicable the difference in cost between Buyer's purchase of Supplier's Goods and replacement Goods. This Section shall apply, without limitation, regardless of whether claimants are contractual counterparties, investors, or any other person, entity, or governmental unit whatsoever.

General commentary to Article 5

1. Introduction

This section provides for remedies in case of a default related to Human Rights and Environmental Due Diligence in accordance with Article 1 or a failure to establish or implement a Remediation Plan in accordance with Article 2.3. Obviously, other types of defaults are conceivable as well, but the presumption here is that they are dealt with elsewhere in the supply chain contract. It is well conceivable that the sections on remedies (5.2, 5.4 and 5.5) are to a large extent also implemented elsewhere in the supply chain contract. However, one should note that Section 5.2 includes some specific elements regarding defaults related to Human Rights and Environmental Due Diligence in accordance with Article 1 or a failure to establish or implement a Remediation Plan in accordance with Article 2.3, for example on responsible exit. Beyond this, section 5.3 is specific to this type of default and will not be provided for elsewhere in the supply chain contract either.

2. Section 5.1

(a) It may be argued the collaboration of Buyer in the remediation of Adverse Impacts would deprive the Buyer from his statutory right to claim damages from the Supplier in case of an Adverse Impact, but this would not be the case. The Buyer has contributed to the Adverse Impact and has an own obligation to compensate the affected individuals. The circumstance these damages are partially paid from the damages the Supplier may have to pay to Buyer does not alter this. That said, such collaboration with Supplier should not be considered to be a waiver of Buyer's rights under Article 5.

(b) One should note that this section uses the term 'corrective action plan'. This term should be discerned from the term 'remediation plan' in Article 2. A remediation plan is also required if no breach of the Agreement has occurred, but an Adverse impact has been observed either at the Supplier level or further down the supply chain. The term 'corrective action plan' is reserved to measures required to cure a breach of the Agreement and not of an Adverse impact. However, if the breach is related to an Adverse impact the corrective action plan may include the remediation plan. Therefore, the term 'corrective action plan' is not always commensurate with this term in Article 8(3)(b) CSDDD.

Under the national contract laws of some member States, it is allowed to invoke the consequences of a breach before it has occurred under specific conditions, for example when the Supplier has announced it will not comply with a specific element of the Agreement, for example the establishment and implementation of a remediation plan. In these systems the consequences of sections 5.1(b)-5.1(f) and 5.2-5.4 may also be invoked to the situation in which a breach is imminent. This may be clarified in these sections.

(e) Buyer has the obligation to collaborate with and support the Supplier to ensure remedy for the affected persons or individual as Article 8(3)(g) of the CSDDD requires and necessary investments to prevent future adverse impacts as Article 8(3)(d) demands.

(f) In some instances, Buyer has required Supplier to source from specific suppliers. If the default occurs at this supplier level, Buyer should see to it that this default is cured. If this is not achieved within the set timeframe or is impossible within that timeframe, Supplier may require Buyer to consent to sourcing from another supplier. Obviously, this may also be a reason for Buyer to terminate the agreement with this designated supplier (under the conditions set forth in Article

1.3(h) on responsible exit), but this would be the sole responsibility and choice of Buyer and not of Supplier. Therefore, it is not logical if Supplier could require Buyer to terminate this agreement.

3. Section 5.2

(a) Seeking for contractual assurances is specifically acknowledged as a means of preventing or addressing environmental and human rights abuse by Articles 7(2)(b) and 8(3)(c) and 8(5) of the CSDDD. Pursuant to Article 8(5) these contractual assurances need to be fair, reasonable and non-discriminatory if a small or medium sized Supplier is involved.

It is also important to meaningfully consult affected individuals or organizations or their representatives when exercising these remedies.[85]

(ii) Some supply contracts will call for payment by letter of credit, which will complicate the right to suspend payment. When a documentary credit is involved, the supply contract and letter of credit should require presentation of a certificate of compliance with the obligations under the Agreement. In any case, the certificate should be required to be dated within a reasonably short time of the draw. Many banks probably will not object to the requirement of an additional certificate as certificates (e.g., by SGS) are commonplace in such transactions, and environmental certificates are similar to (and in some cases may be the same as) a certificate of compliance with the Agreement. While some banks may resist the requirement of such a certificate because of fear of injunction actions and the concomitant extension of the credit risk if the injunction is ultimately denied, most banks seem unlikely to be concerned by the requirement of one more certificate, and any additional credit risk from an injunction may be mitigated by a bond or other credit support by the civil procedure laws or rules of certain jurisdictions requiring posting of a bond, or by collateralization or bonding provisions in the reimbursement agreement itself. Still, despite all of these efforts, suspension of payment may be impossible in cross-border documentary credit transactions because frequently a foreign bank will have honored before the injunction can issue.

(iii) As is elaborated in Article 1.3 termination should result in a responsible exit. This section may not be understood as to support a ‘ hit and run’ strategy, meaning immediate termination by Buyer if a Schedule P breach is identified and neglecting the Buyers responsibilities regarding remediation for those individuals affected. In order to strengthen this obligation of Buyer one may introduce a rebuttable presumption that termination will not be responsible if Buyer has contributed to the Schedule P breach. More generally speaking in seeking certain of the remedies provided for (e.g. termination of agreements, removal of employees, suspending payments), it should be noted that it will be important for the enforcing party to consider any potential adverse human rights impacts of such actions which could compound existing adverse impacts (as contemplated in proposed clauses 1.3(f), 2.5 and 3.3).

Beyond this, the EU directive on unfair trade practices in agricultural supply chains[86] does not allow short-term termination of agreements regarding fungible goods, although member states may allow an exemption if these goods can reasonably be sold elsewhere.[87] Furthermore, Article 3(1)(h) Unfair

[85] Articles 6a, 8(3)(b) and Recital 26a CSDDD.
[86] Directive EU 2019/633.
[87] Article 3 section 1 and considerations 17 and 20 of the directive.

Trade Practices Directive in agricultural supply chains prohibits retaliation against the supplier, for example, by reducing or cancelling orders. Therefore, if termination is considered to be retaliation it is not allowed under this directive.

One should note that several European legal systems allow for termination for breach without notice under specific conditions, for example in case of irreversible damage.

(iv) In connection with damages it is important to note that Article 8(3)(a) of the CSDDD requires the compensation of affected individuals or affected communities. The Buyer should see to it this is actually implemented and should even pay (part of) these damages in cases in which the Buyer has contributed to these adverse impacts as envisaged in section 5.1(a). This is also contemplated in section 8(3)(g) of the CSDDD.

4. Section 5.3

(a) It is important that neither Buyer nor Supplier benefit from an Adverse Impact. For example, if Buyer orders additional goods with a very short lead time which foreseeably causes excessive overtime being made by Supplier's workers, this may result in a profit for the Buyer being able to sell more goods with a good margin. However, when claiming damages from Supplier because of the noncompliance with obligation to address this Adverse Impact, this profit should be taken into account, especially in connection with the compensation which should be paid to Supplier's workers and in which the Buyer has a responsibility because of its contribution to the Adverse Impact.

(b) In connection with damages it is important to note that Article 8(3)(g) of the CSDDD requires the compensation of affected individuals or affected communities. Buyer should see to it this is actually implemented and should even pay (part of) these damages in cases in which the Buyer has contributed to these adverse impacts as envisaged in Section 5.1(a). The compensation of affected persons/communities should prevail over the damages the Buyer may claim from the Supplier and, thus, as long as the Supplier avails over insufficient funds to compensate the damages of both the affected persons/communities and of the Buyer, the Buyer should accept the affected persons/communities being compensated first. This section includes such a provision.

For example, if Supplier agrees to a change order requested by Buyer and the parties should know that Supplier will be unable to perform without the occurrence of Adverse Impacts, indemnification to Buyer must be reduced to the extent, pro rata, that Buyer caused or contributed to the harm. This clause sets up a mechanism akin to a comparative fault regime.

Here third-party beneficiary rights may be implemented. See the practical guidance to Article 2.3 for an example of a clause granting these rights.

5. Section 5.4

It may be considered to not destroy the goods which have been produced with a Schedule P breach but sell them and use the proceeds to compensate those individuals affected by this breach.

Practical guidance to Article 5

1. Section 5.1

(a) The definition of a contribution of Buyer to environmental impact may have to different from direct human rights impact. Therefore, it may be helpful to further define contribution to environmental impact.

(b) Art. 2(m) of the Conflict Minerals Regulation includes a specific provision on certification, which may be approved by the European Commission if a certification scheme meets the OECD due diligence guidance and pass the OECD alignment test. It may be advisable to use the presumption of undertaking sufficient human rights due diligence if an (approved) certification scheme or designated multi-stakeholder initiative is implemented by small or medium sized enterprises. If a certificate is withdrawn, this may trigger a rebuttable presumption that the Supplier is in Default. Such a presumption may be embedded in the contract.

Member State specific comments to Article 5, UK and DCFR

1. France

The article seems commensurate with Article 1231 of the French Civil Code.

2. Germany

In principle, due to the principle of party autonomy, parties may agree on the terms of their contract including on the remedies. Hence, agreements as to the remedies are possible to the extent that they do not disproportionately disadvantage one of the parties. The structure of remedies under German civil law is organized to prioritize specific performance (s. 439 German Civil Code) with other typical sales law remedies (recission, price reduction damages) being subject to additional conditions. Against this background, some of the remedies could be interpreted as being subject to additional requirement. This applies to withdrawal from the contract, which is subject to the condition that the defaulting party to the contract declares not to perform or the non-defaulting party having given a deadline for performance of the contract that has passed. In a sales contract, the non-defaulting/innocent party can, instead of withdrawing from the contract, claim price reduction (§ 441 BGB).

When it comes to damages, German law requires fault or intention to apply the remedies provided for in Article 5 (§ 280 (1) 2).

3. Italy

It is important to note that according to Italian law, the terms 'fault' and 'intentionally' should be replaced with the terms negligence (*colpa*) and wilful misconduct (*dolo*), referred to in the applicable Italian contractual liability law.

Section 5.2(e): Under Italian law compensation for damages for non-performance or delay shall include the damages (*danno emergente*) suffered by the creditor as well as the loss of profit (*lucro cessante*), insofar as they are an immediate and direct consequence of the breach.
Beyond this, if the non-performance or delay is not due to the debtor's willful misconduct, the compensation shall be limited to the damage that could have been foreseen at the time when the obligation arose. Finally, in the event of breach of an agreement, not only pecuniary damages but also non-pecuniary damages may be compensated.
Pursuant to Section 1229 of the Italian Civil Code, any *ex ante* limitation of the liability of a party for damages caused by intentional misconduct (*dolo*) or gross negligence (*colpa grave*) is null and void. This might potentially be in contrast, for instance, with the principle that remediation should have priority over the payment of damages in case of intentional or grossly negligent breach of contract that also resulted in an Adverse Impact.

4. Poland

Limits on interpretation/modification by conduct will be valid and enforceable as long as they are not used to endorse an unconscionable, inconsistent conduct.

Section 5.1: this section provides for no informal modification in the matters concerned. This section may well serve as 'lex specialis' to any modification rules in the supply chain agreement, which may be more liberal and therefore inappropriate here.

5. Portugal

Sections 5.3(a) and 5.3(b): The broadness of these provisions may give rise to serious unintended consequences, notably as a reimbursement or compensation would need to be awarded by reference to specific losses and damages evidenced by the non-breaching party. Thus, the commitment to have those amounts be redirected to remediation processes may leave the non-breaching party in a worse position and, concomitantly, work as an unlawful limitation to the right of a party to access legal remedies available to it or to terminate the agreement by breach.

Section 5.3(c): In Portugal courts are entitled to reduce the liquidated damages provision if it is deemed to be unreasonable in light of the damages and losses effectively evidenced before the court.

6. Spain

Sections 5.2 and 5.3: according to article 1.102 of the Spanish Civil Code, any limitation of liability (either as regards the amount or the capacity to claim it) is not enforceable when the party who claims the limitation acted with wilful intent ("dolo").

Under Spanish law, absent wilful intent ("dolo") the parties can agree on a specific amount to be claimed in case of breach of a specific clause or undertaking provided that such amount is not disproportionate (in which case the Judge, under certain circumstances, can moderate the amount). In addition to this, the parties shall bear in mind that the Spanish Civil Code only refers explicitly to actual damages suffered as a consequence of a breach of contract ("daño emergente") and loss of profit ("lucro cesante") and that the concepts of consequential and indirect damages, if used, are ambiguous and open to interpretation, without the Spanish case law having clarified their content.

Regarding Section 5.2 (b), it must be taken into account that, under the Spanish Procedural Act, if the Buyer files a request for interim measures, the Buyer will be obliged to file a claim before the Spanish Courts within the following month after the adoption of the interim measures. This provision could be somehow in contradiction with the Dispute Resolution Procedures set out in Article 7.

Section 5.4: Further to the principle of freedom of contract of article 1255 of the Spanish Civil Code, a contractual undertaking contemplating the destruction or donation of goods would be lawful without an instruction of Supplier or without prior written notification in advance to Supplier, unless in the particular circumstances surrounding the enforcement of such clauses the affected party could prove that the other party has breached the general obligation to perform the contract in good faith, although according to Spanish case law this is a proposition which would be very difficult to successfully argue before a Spanish Judge.

In addition to this, sections 5.4 (b) and (c) would also be lawful under Spanish law.

7. UK

Section 5.2(a): The proposed wording 'adequate assurances of performance' has no special meaning under English law, but in context it makes sense and appears to adequately convey the intended meaning.

Section 5.2(b) and 5.2(c): The Buyer's proposed remedies include obtaining an injunction with respect to Supplier's noncompliance with Schedule P (clause 5.2(b)); and requiring a Supplier to terminate an agreement or affiliation with a specific factory, to terminate a subcontract or to remove employees/other representatives (clause 5.3(c)).[88] Under UK law it is recommended to amend the drafting of clause 5.2(b) to refer to '*specific performance*[89] *and/or an injunction';* and to refer to the parties' agreement that '*damages would not be an adequate remedy'* for breach.

However, it is important to note that a Buyer may face challenges in seeking to enforce these rights/remedies. This is because injunctions and specific performance are discretionary remedies that are not available as of right. For instance, these remedies would not typically be granted if the relevant terms are too uncertain/imprecise for a clear order to be made; where ongoing supervision/oversight would be required; and/or where damages would be an adequate remedy (amongst other considerations).

The proposed drafting tweaks above would reduce the likelihood of a court/tribunal considering that damages are an adequate remedy. However, there may well still be difficulties in obtaining an order requiring a Supplier to comply with certain obligations (e.g. in connection with human rights due diligence/compliance with Schedule P/the preparation and implementation of a Remediation Plan) because of the issues flagged above.

Section 5.3: Under English law a penalty clause (i.e. a sum which is not a reasonable pre estimate of the other parties' loss), is not enforceable. Therefore, from an English law perspective, it is suggested deleting 5.3(c).

8. Draft Common Frame of Reference (DCFR)

The remedies envisaged in Section 5.2 are commensurate with the DCFR. Especially section 5.2(b) with Article III-3:302, section 5.2(d) with Article III-3:502 and section 5.2(e) with Article III-3:701.

However, termination is envisaged in Article III-3:502 if a fundamental breach has occurred. Whereas this does not have to be the result of a Zero Tolerance Activity, the EMCs restrict termination, in line with the CSDDD, further than the DCFR envisages.

Section 5.2(a) relates to Article III-3:505 which allows the Buyer to ask for adequate assurances and if not provided grants the right to terminate. However, as explained hereinabove such termination should be responsible.

Article III-3:704 and III-3:705 also explicitly acknowledge the right to damages of the Buyer may be reduced if Buyer has contributed to these damages or could have taken reasonable steps to reduce the loss of the Supplier.

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88 This may raise labour law issues which are not further considered here.

89 Specific performance is an order compelling a party to perform positive contractual obligations.

Article 6 Extent of Buyers Duties

6.1 Negation of Buyer's Contractual Duties Except as Stated

Notwithstanding any other provision of this Agreement:

(a) Buyer does not assume a further reaching duty under this Agreement to monitor Supplier or its Representatives, including, without limitation, for compliance with laws or standards regarding working conditions, pay, hours, or the like, then required by Buyer's obligations under Articles 1 and 2, unless such further reaching duty is required under applicable law and to the extent it is required by applicable law.

(b) Buyer does not assume a further reaching duty under this Agreement to monitor or inspect the safety of any workplace of Supplier or its Representatives nor to monitor any labor practices of Supplier or its Representatives, then required by Buyer's obligations under Articles 1 and 2, unless such further reaching duty is required under applicable law and to the extent it is required by applicable law.

(c) Buyer does not have a further reaching authority and disclaims any further reaching obligation to control (i) the manner and method of work done by Supplier or its Representatives, (ii) implementation of safety measures by Supplier or its Representatives, or (iii) employment or engagement of employees and contractors or subcontractors by Supplier or its Representatives then required by Buyer's obligations under Articles 1 and 2 or if such further reaching obligation is required under applicable law and to the extent it is required by applicable law. The efforts contemplated by this Agreement do not constitute any authority or obligation of control, unless such obligation is required under Articles 1 and 2 or applicable law and to the extent it is required by applicable law. They are efforts at cooperation that leave Buyer and Supplier each responsible for its own policies, decisions, and operations. Buyer and Supplier and Representatives remain independent and are independent contractors. Nor are they joint employers, and they should not be considered as such.

(d) If Buyer makes use of audits to verify compliance with this Agreement by Supplier and such audits are commensurate with Section 1.3(i), Buyer shall bear the cost of such audits if Supplier is an SME. If Supplier is not an SME and an audit is commensurate with Section 1.3(i) the cost of this audit is borne by [Buyer][Supplier].

General commentary to Article 6

1. Introduction

This article limits the responsibilities of Buyer, but still requires Buyer to take all measures and control over Suppliers activities as required to undertake proper Human Rights and Environmental Due Diligence as required by Articles 1 and comply with its obligations under Article 2. This seems counterintuitive bearing in mind the elaborate requirements in Articles 1 and 2 to collaboratively deploy human rights and environmental due diligence. However, it is not. Suppliers are generally reluctant to accept control over their activities.[90] This Article clarifies control by Buyer may not exceed the control needed to comply with Articles 1 and 2. Beyond this, more extensive control may also be contrary to contract law in several countries.[91]

2. Section 6.1

(b): It should be noted this clause should not be used to restrict the right to safety of workers or to deteriorate working conditions.

(b) and (c): Competition issues may emerge if these sections are removed. For example, agreement with competitors over payment of certain wages may be an issue. However, in vertical agreements this issue may be less salient.[92]

(c) this section clarifies that Buyer has no obligation to control or monitor Supplier unless this is required to implement and undertake environmental and Human Rights and Environmental Due Diligence as required by Article 1 and to meet its obligations under Article 2.

(d) This section is required by Articles 7(4) and 8(5) CSDDD as far as Supplier is an SME. If not, parties are free to choose whether Supplier or Buyer pays for the audits. One should realize that audits are just a snapshot in time and can, therefore, not be the only means to assess whether Supplier has implemented proper human rights and environmental due diligence.[93]

[90] See e.g. BAFA Guidance ("Zusammenarbeit in der Lieferkette zwischen verpflichteten Unternehmen und ihren Zulieferern - Die wichtigsten Fragen und Antworten für KMU", 1ed June 2023), p. 21.
[91] See BAFA Guidance ("Zusammenarbeit in der Lieferkette zwischen verpflichteten Unternehmen und ihren Zulieferern - Die wichtigsten Fragen und Antworten für KMU", 1ed June 2023), p. 21.
[92] See on this e.g. BAFA Guidance ("Zusammenarbeit in der Lieferkette zwischen verpflichteten Unternehmen und ihren Zulieferern - Die wichtigsten Fragen und Antworten für KMU", 1ed June 2023), p. 32.
[93] Cf. BAFA Guidance ("Zusammenarbeit in der Lieferkette zwischen verpflichteten Unternehmen und ihren Zulieferern - Die wichtigsten Fragen und Antworten für KMU", 1ed June 2023), p. 16.

Member State specific comments to Article 6, UK and DCFR

1. France

2. Germany

3. Italy

4. Poland

5. Portugal

6. Spain

Section 6.1 (a): under article 42 of the Spanish Workers' Statute, companies who subcontract their own activity must obtain a certificate stating that the relevant supplier has no pending debts with the Social Security. Otherwise, the client will be jointly and severally liable with the supplier for the latter's obligations with the Social Security during the term of the agreement and three years thereafter.

Section 6.1(c): under Spanish law the exclusions associated with labour matters are lawful and advisable. However, although the terms of the supply agreement can be considered as an indication, for the assessment on whether there is a labour relationship between the Supplier's employees and the Client, the courts will consider the actual facts of the relationship irrespective of the provisions included in the agreement.

7. UK

It is not typical to see disclaimers of this length and/or nature in UK agreements. One would expect the Buyer's responsibility to be framed through positive obligations (for example, including a right for the Buyer to monitor and audit compliance with the terms imposed). There is also the potential that despite such provisions seeking to limit the duties imposed on the Buyer, given the extent of the wider provisions and obligations placed on the Supplier that a duty could be found to exist in any subsequent litigation.

8. Draft Common Frame of Reference (DCFR)

Article 7 Dispute Resolution

7.1 Dispute Resolution Procedures

The parties agree that, except for emergency measures, the procedures set forth in this Article shall be the sole and exclusive remedy in connection with any dispute arising in whole or in part from or relating to Articles 1 through 6 [or Schedule Q], whether such dispute involves Buyer, Supplier, or a Representative (a "Dispute"). Buyer and Supplier irrevocably waive any right to commence any action in or before any court or governmental authority, except as expressly provided in this Article 7. Notwithstanding anything contained herein to the contrary, however, at any point in the proceedings under this Article 7, the parties may agree to engage the services of a neutral facilitator to assist in resolving any Dispute.

7.2 [Confidentiality

All documents and information concerning the Dispute, including all submissions of the parties, all evidence submitted in connection with any proceedings, all transcripts or other recordings of hearings, all orders, decisions and awards of the arbitral tribunal and any documents produced as a result of any informal resolution of a dispute, shall be confidential, except with the consent of both parties or where, and to the extent, disclosure is required of a party (a) by legal duty, (b) to protect or pursue a legal right, or (c) in relation to legal proceedings before a court or other competent authority.]

7.3 Joinder of Multiple Parties

If one or more other disputes arise between or among parties to other contracts that are sufficiently related to the same or similar actual or threatened human rights violations, the parties shall use their best efforts to consolidate any such related disputes for resolution under this Article 7.

7.4 Informal Good Faith Negotiations Up the Line

The parties shall try to settle their Dispute amicably between themselves by good faith negotiations, initially in the normal course of business at the operational level. If a Dispute is not resolved at the operational level, the parties shall attempt in good faith to resolve the Dispute by negotiation between executives who hold, at a minimum, the office(s) of [TITLE(S)]. Either party may initiate the executive negotiation process at any time and from time to time by providing notice (the "Dispute Notice"). Within no more than five (5) days after the Dispute Notice has been given, the receiving party shall submit to the other a written response (the "Response"). The Dispute Notice and the Response shall include (a) a statement of the Dispute, together with a recital of the alleged underlying facts, and of the respective parties' positions and (b) the name and title of the executive who will represent that party and of any other person who will accompany the executive. The parties agree that such executives shall have full and complete authority to resolve the Dispute. All reasonable requests for information made by one party to the other will be honored. If such executives do not resolve such dispute within [twenty (20)] days of receipt of the Dispute Notice for any reason, the parties shall have an additional [ten (10)] days thereafter to reach agreement as to whether to seek to resolve the Dispute through mediation under Section 7.6.

7.5 Expert Determination and Assessment

Parties may agree to engage experts for expert determination or assessment of fact. If Parties have agreed to engage (an) expert(s) they will negotiate in good faith regarding the appointment of one or more experts. Parties will share the cost of the determinations and/or assessments by such experts and will, upon request by the expert(s), provide information to the expert(s) which the expert(s) reasonably need to undertake the determination and/or assessment Parties have agreed upon. Expert(s) shall enable Parties to review and comment on their draft findings and will respond to the comments of the Parties regarding the draft findings.

7.6 Mediation

If the parties do not resolve any Dispute within the periods specified in Section 7.4, either party may, by notice given in accordance with Section 2.3(b) or 5.1(b)(the "Mediation Notice"), invite the other to resolve the Dispute under the [insert name of rules] as in effect on the date of this Agreement (the "Mediation Rules"). The language to be used in the mediation shall be [language]. If such invitation is accepted, a single mediator shall be chosen by the Parties. If, within [_____] days following the delivery of the Mediation Notice, the invitation to mediate is not accepted, the parties shall resolve the Dispute through [arbitration][litigation] under Section 7.7] [If the parties are unable to agree upon the appointment of a mediator, then one shall be appointed by the [insert title of official at the named institution]].

7.7 [In this clause, companies choose between arbitration (Alternative A) and litigation (Alternative B):] [Arbitration] [Litigation]

If and only if the parties (a) have chosen not to make use of Mediation under Section 7.5 to resolve the Dispute, or (b) have not, within [____] days following the delivery of the Dispute Notice, resolved the Dispute using such Mediation, then the Dispute shall be settled

[Alternative A for arbitration:] [by arbitration in accordance with the [name of rules of the arbitration institution] (the "Arbitration Rules") in effect on the date of this Agreement. The number of arbitrators shall be [one] [three]. The seat of arbitration shall be [seat] and the place shall be [place]. The language of the proceedings shall be [language]. [The provisions for expedited procedures contained in [section or article] of the Arbitration Rules shall apply irrespective of the amount in dispute. The parties further agree that following the commencement of arbitration, they will continue to attempt in good faith to reach a negotiated resolution of the Dispute.]

[Alternative B for litigation:] [by the District Court of ____ [here refer to the choice of forum, preferably in an EU member state] which has exclusive jurisdiction, for any dispute, in connection with this agreement, with the exclusion of any other place of jurisdiction].

7.8 [Only for use with Alternative A for arbitration:] [Emergency Measures

Notwithstanding any provision of this Agreement or any applicable institutional rules, any party may obtain emergency measures at any time to address a Zero Tolerance Activity or any other imminent threat to health, safety, or physical liberty. In addition, a party may make an application for emergency relief to the [name of institution] (the "Arbitration Institution"] for emergency measures under the arbitration rules of the Arbitration Institution as in effect on the date of this Agreement.]

7.9 [Only for use with Alternative A for arbitration:] [Arbitration Award

The arbitrator(s) may grant any remedy or relief set forth in Article 5 or elsewhere in this Agreement and that a court of competent jurisdiction could grant, except that the arbitrators may not grant any relief or remedy greater than that sought by the parties, nor any punitive damages. The award shall include compliance with a Remediation Plan as contemplated by Article 2.3 above. [The arbitration tribunal shall send a copy of each final order, decision and award to [title of official and name of institution] so that the public may have access to such documents, provided that, prior to sending any such document to such repository, such arbitration tribunal, in consultation with each of the parties, shall redact any information from such document that would (a) would reveal the identity of any party that wishes to remain anonymous; or (b) disclose any other information (including without limitation the amount of any award, any proprietary information or any trade secrets) that a party wishes to remain confidential.]]

7.10 Applicable Law

This Agreement shall be governed (including its validity, interpretation and effects) exclusively by the Laws of *[recommended: the law of an EU Member State*], without regard to the conflict of Laws provisions thereof.

General commentary to Article 7

1. Introduction

The dispute resolution options in this article should be considered in light of the dispute resolution clauses in a sales contract. Article 7 may or may not be suitable for all applications and should be considered in the context of Buyer's existing internal policies and Buyer's customary contractual terms regarding the resolution of disputes and claims, including Buyer's standard form and template procurement agreements; the standard terms and conditions of Buyer's purchase orders; and the Buyer's supplier codes of conduct or analogous documents that include, inter alia, administrative, operational, remedial and/or corrective action procedures, processes, sanctions, and penalties. Dialogue, settlement, and remediation of any controversy arising from a human rights abuse offer victims the most favorable and expeditious resolution, but it is also possible that both human rights abuse and other contractual breaches could be involved. The corporate culture of a company will likely determine whether arbitration or litigation is the preferred route to follow for breaches, provided that under no likely circumstance would a party agree to bifurcate its chosen resolution of such multiple disputes. A mediation during-the pendency-of litigation clause is therefore included here.

2. Section 7.1

This Agreement explicitly provides that every supplier and buyer in the chain is bound to prevent or mitigate Adverse Impacts. Involvement of Representatives (further down the supply chain) in dispute resolution is therefore contemplated in this clause.[94] It is also relevant to consult affected stakeholders in connection with this dispute resolution, as this is required by the CSDDD (and the German Supply Chain law), although it is not necessary per se that these stakeholders also become a party in this dispute resolution. That said, it may be considered to make them party to the dispute if they accept this assignment.

3. Section 7.2

Confidentiality is usually perceived as among the advantages of arbitration, including international commercial arbitration, over litigation and public filings. Confidentiality comes with drawbacks, however, particularly where the proceeding affects the public interest, as is likely true when a dispute relates to human rights. This provision is bracketed, and the parties should carefully negotiate and omit or adapt the text to reflect the form of confidentiality or transparency that best suits their efforts to mediate or arbitrate. Note that the UNGPs do not require full transparency. UNGP 31(e) expects that nonjudicial grievance mechanisms will keep parties informed and 'provid[e] sufficient information about the mechanism's performance to build confidence in its effectiveness and meet any public interest at stake.' The commentary states, 'Communicating regularly with parties about the progress of individual grievances can be essential to retaining confidence in the

[94] See e.g. generally International Chamber of Commerce Rules of Arbitration, art. 7 (2017) ("Joinder of Additional Parties").

process. Providing transparency about the mechanism's performance to wider stakeholders, through statistics, case studies or more detailed information about the handling of certain cases, can be important to demonstrate its legitimacy and retain broad trust. At the same time, confidentiality of the dialogue between parties and of individuals' identities should be provided where necessary.' This is also contemplated in Article 6a and 8(3)(b) as well as Recital 26a of the CSDDD. The Hague Rules on Business and Human Rights (BHR) Arbitration[95] call for transparency of all proceedings. The Hague BHR Rules aim to fill the judicial remedy gap in the UNGPs and should be considered by those companies committed to the UNGPs. In any case, those who are not legally required to disclose discovered human rights abuses and who hope to protect any Dispute from public dissemination, especially before cure or remediation is in place, must verify the applicable chosen rules regarding confidentiality or should include express provisions in the arbitration provisions that deal with confidentiality. This section requires total confidentiality unless otherwise required. The bracketed portion of Section 7.9, however, allows for an agreed upon release of redacted final orders and awards.

4. Section 7.4

The number of days mentioned in this section appropriate for good faith negotiations may vary based on the severity or breadth of the Adverse Impact as well as Buyer's ability to find another source for the products at issue.

A commitment to engage in mediation need not be complex, and these Model Clauses use the short and simple clauses recommended by such institutions as the PCA and UNCITRAL. Other institutions that provide mediation services may not accept clauses such as these, and the drafter should consult with such other institutions to determine what text to employ.[96]

5. Section 7.6

It should be noted that the European Union has issued a directive on transboundary mediation, which is relevant for this in 2008.[97] A further relevant document is the European code of conduct for mediators of 2009.[98] However, it may be questionable whether all human rights and workers issues can be mediated under European law.

[95] Which can be accessed at https://www.cilc.nl/cms/wp-content/uploads/2019/12/The-Hague-Rules-on-Business-and-Human-Rights-Arbitration_CILC-digital-version.pdf.

[96] Reference should be made to Model Arbitration Clauses for the Resolution of Disputes under Enforceable Brand Agreements at https://laborrights.org/sites/default/files/publications/%20Model%20Arbitration%20Clauses%20for%20the%20Resolution%20of%20Disputes%20under%20Enforceable%20Brand%20Agreements.pdf. See also Clean Clothes Campaign et al., Model Arbitration Clauses for the Resolution of Disputes under Enforceable Brand Agreements, Int'l Lab. Rts. F. (June 24, 2020), https://laborrights.org/publications/model-arbitration-clauses-resolution-disputes-under-enforceable-brand-agreements.

[97] Accessible at https://eur-lex.europa.eu/legal-content/EN/ALL/?uri=celex%3A32008L0052.

[98] Accessible at http://www.euromed-justice-iii.eu/document/eu-european-code-conduct-mediators.

6. Section 7.7

In selecting the applicable Arbitration Rules, the parties must be sure the scope of discovery and the cost allocation are acceptable and can add text deviating from what is provided within such provisions if not. However, it may be questionable whether all human rights and workers issues can be arbitrated under European law.

The arbitration alternative A is derived from 8 The Singapore Arb-Med-Arb Clause:[99] "Arb-Med-Arb is a process where a dispute is first referred to arbitration before mediation is attempted. If parties are able to settle their dispute through mediation, their mediated settlement may be recorded as a consent award. The consent award is generally accepted as an arbitral award, and, subject to any local legislation and/or requirements, is generally enforceable in approximately 150 countries under the New York Convention. If parties are unable to settle their dispute through mediation, they may continue with the arbitration proceedings."

If the parties do not wish to include mediation and/or arbitration provisions, the Model Clauses assume somewhere in the underlying master agreement they have included standard text addressing litigation issues such as the choice of law and choice of forum, consent to jurisdiction and service of process; these litigation provisions are not included in these Model Clauses.

If Alternative B for litigation is chosen, the insertion of a clause on the choice of forum providing for the jurisdiction of the courts of an EU Member State is recommended. This choice is important in the perspective of art. 22(5) of the CSDDD, about civil liability for human rights and environmental damages, according to which "[..] the liability provided for in provisions of national law transposing this Article is of overriding mandatory application in cases where the law applicable to claims to that effect is not the law of a Member State".

7. Section 7.8

Several standard arbitration systems contemplate a financial harm ceiling for the application of expedited procedures, which will not be applicable in the context of the discovery of human rights abuses where the harm is not necessarily or primarily a financial harm to be suffered by one of the parties. The following alternate wording could be added: "The provisions for expedited procedures contained in the Arbitration Rules shall apply, provided the discovered harm is ongoing and steps to immediately address and cure are possible but not being voluntarily implemented."

8. Section 7.10

It is recommended that the parties choose the law of an EU Members State as the law governing the agreement, through the insertion of an *ad hoc* clause. This also triggers the applicability of the CSDDD.

If this clause is not introduced and/or the applicable law is the law of a third country (in accordance with the rules of private international law followed by the court), in principle the rules on Human Rights and Environmental Due Diligence established in compliance with the CSDDD do not apply,

[99] Accessible at https://siac.org.sg/model-clauses/the-singapore-arb-med-arb-clause.

with the exception provided for by art. 22(5) of the CSDDD regarding civil liability for human rights and environmental damages ("[…] the liability provided for in provisions of national law transposing this Article is of overriding mandatory application in cases where the law applicable to claims to that effect is not the law of a Member State"). In this latter regard, see Article 7.7 and General Commentary to Article 7 - Section 7.7 above, for the same approach in terms of choice of forum.

Practical guidance to Article 7

One should note that if third-party beneficiary rights are granted in accordance with the practical guidance provided with Article 2.3, these third parties should also have a role in this dispute resolution clause.

Member State specific comments to Article 7, UK and DCFR

1. France

Section 7.1: It is important to bear in mind Articles 54, 58, 131(1), 1532 and 1565 of the Code of Civil Procedure (CCP), which impose specific requirements on arbitration, mediation and litigation. Furthermore, if a specific human rights or environmental issue is considered to be of an administrative nature Articles L-R. 213 ff. of Décret n° 2017-566 of 18 April 2017 include rules on such administrative mediations.[100] Furthermore, not all human rights and workers rights issues are amenable to mediation or arbitration under French law. Beyond this, the distinction and boundaries between mediation, arbitration and litigation may not be clear and should be clarified.
Section 7.7: Arbitration is governed by Articles 1474 ff and 2061 CCP.

2. Germany

Section 7.7: German civil procedure law has specific rules on arbitration agreements in §§ 1025 ZPO et. seq. Pursuant to Section 1030 of the Code of Civil Procedure, property disputes may be the subject of an arbitration agreement. Non-property disputes can be settled in an arbitration agreement insofar as the parties are entitled to reach a settlement on the subject of the dispute. Thus, e.g. matrimonial and child matters are not arbitrable. Arbitrability is affirmed for disputes about violations of general rights of personality ("Persönlichkeitsrechte"). There is no clear, definitive list in Germany of the matters that cannot be submitted to arbitration.

A special feature of German law is § 1027 ZPO, according to which a violation of a non-mandatory provision or a violation of a procedural requirement agreed upon by the parties must be noted immediately in the arbitral proceedings. Otherwise, this procedural violation is precluded.

Section 7.8: Arbitral tribunal may order interim or protective measures at the request of a party. It should be noted that according to § 1033 ZPO, an arbitration agreement does not preclude a court from ordering a provisional or protective measure in respect of the subject matter of the dispute. Parties cannot derogate from this rule. Courts can enforce interim or protective measures by an arbitral tribunal, unless such a measure is already filed with a court under § 1033 ZPO.

Additionally, under requirements of stakeholder engagement under Sec. 4 (4) of the German Supply Chain law and under the CSDDD, it is advisable to include requirements on the participation of rights holders when remedial measures for adverse human rights impacts are agreed upon in arbitration.

[100] Furthermore Articles 127 ff Code Civil also include rules on mediation.

3. Italy

Section 7.2: Under Italian law, all documents filed by the parties in the context of litigation proceedings are confidential. However, *(i)* decision of Italian Courts (as well as of European Courts) – usually duly redacted – may be published *ex officio* on the judicial repositories in order to be consulted by the public, depending on their impact and relevance on the shaping of the legal system and *(ii)* the rendering of the final discussion is usually public, unless the Judge orders that it shall be held privately due to security issues, public order or common decency ("*buon costume*").

Section 7.6: Under Italian law, in order to be valid and enforceable, the choice of forum and the arbitral clause shall be specifically approved by the parties pursuant to articles 1341 and 1342 of the Italian Civil Code ('*doppia sottoscrizione*') as vexatious clauses ('*clausole vessatorie'*) to the extent the agreement is drafted unilaterally by one of the parties without actual negotiation.
An arbitration clause is valid, insofar as the parties do not dispose of their own human rights, but submit to arbitration a contractual dispute that originates from a breach of human rights of a third party, which – in turn – affected their contractual and commercial relation. Indeed, pursuant to article 806 of the Italian Code of Civil Procedure, non-disposable rights ('*diritti indisponibii'*; *e.g.*, health, physical integrity, freedom etc.) may not be referred to arbitration; as just explained, this restriction would not be applicable in the context of this Section 7.6 as long as the non-disposable rights affected are those of the parties to the agreement.
The inclusion of a specific choice-of-law and forum clause may potentially lead to that clause being considered as having a scope limited only to the human rights standards and ethical practices agreed upon therein.

4. Poland

Section 7.1: Under Polish law all cases which can be settled privately by the Parties are arbitrable. This includes private law aspects of human rights violations. Importantly, employment disputes can only be referred to arbitration in a compromise (an agreement to arbitrate concluded only after the dispute arose). Waiver of 'any right to commence any action in or before any court or governmental authority, except as expressly provided in this Article 7' will be ineffective in as far as it would prevent access to public law remedies. The right to challenge an arbitral award issued in proceedings seated in Poland through setting aside proceedings cannot be waived. Nor can the right to oppose enforcement of a foreign arbitral award in Poland. However, in both cases the grounds for challenging the arbitral award are very limited. It may be advisable to include a clause obliging the parties to include identical dispute resolution clauses in upstream and downstream contracts to render a joinder of parties and cases possible/easier.

Section 7.3: The option to join parties to a dispute depends on the applicable rules of procedure. It can be particularly challenging under most common commercial arbitration rules.

Section 7.7: If litigation is initiated in disregard of a valid mediation agreement, the court refers the parties to mediation (but the proceedings are validly issued). As far as arbitration is concerned, failure to exhaust pre-arbitral steps is normally not considered an obstacle to initiate arbitral proceedings in Poland, although the issue is not clear and decisions vary from mere cost sanctions to rejecting a claim not preceded by the exhaustion of pre-arbitral steps 'without prejudice'. The

wording proposed in this section suggests that a dispute is not 'arbitrable' before pre-arbitral stages are exhausted and a claim submitted prematurely should be rejected by the arbitrators 'without prejudice'. This will not necessarily be followed by the arbitrators, who may choose to proceed with the claim regardless and only sanction the claimant with costs, if they consider his decision to initiate arbitration without exhausting pre-arbitral steps unconstructive.

Consent judgments are not envisaged in Polish court proceeding (but are often issued in arbitration). In court proceeding a settlement can be concluded before the court, included in the court record and enforced. However, it is not a court judgment for the purposes of enforcement abroad.

Section 7.8: Under Polish law application to a common court for interim relief is always available, even if parties chose arbitration in the agreement.

5. Portugal

6. Spain

Section 7.1: According to section 2 of Spanish Law on Civil and Mercantile Mediation, employment matters cannot be subjected to mediation, nor any matter involving criminal law or mediation with public administrations.

Submission to arbitration is lawful under Spanish law and the arbitration award is deemed to be final unless, according to section 41 of the Spanish Arbitration Law, there have been defects in the arbitration proceedings notifications, the arbitrators have decided on matters beyond their power to decide, the arbitration proceedings are inconsistent with what the parties have agreed in the contract clause establishing the arbitration (unless such agreement is contrary to Law), the arbitrators have decided on matters which cannot be subject to arbitration or the award is against Spanish public order, in which case the arbitration procedure and the arbitration award can be challenged before the Spanish Courts.

Other than the above, the parties can agree on submitting their disputes to good faith negotiations, mediation and/or arbitration.

7. UK

The proposed dispute resolution clauses will need to be considered in the context of any dispute resolution provisions in the main sales agreement. The clauses appear to contemplate that the parties may include separate litigation/arbitration provisions in the main sales agreement; and the clauses set forth herein (see, e.g., section 7.7). In principle, it is possible to have multiple dispute resolution mechanisms. However, this could give rise to significant difficulties and the risk of parallel proceedings (for instance, where a dispute relates to the main provisions of the sales contract and the clauses set forth herein), so would need to be considered carefully in any given case.

Section 7.2: There is no barrier to the parties agreeing on the confidentiality of arbitration proceedings under English law.

Section 7.7: If the parties opt for arbitration, the efficacy and drafting of relevant proposed clauses will need to be considered in light of the arbitral institution/rules selected (i.e. including the clauses in relation to confidentiality (as included in section 7.2), joinder of multiple parties (as set forth by section 7.3) and emergency arbitration (implemented in section 7.8).

Section 7.8: It is not possible to guarantee that interim/emergency relief – whether from an emergency arbitrator or the courts – would be granted through providing for this in the contract. An English court could only grant relief in support of arbitral proceedings (with a seat in London) if/to the extent that the tribunal/institution has no power or is unable to act effectively.

Section 7.9: It is not possible to guarantee that a final arbitration award will provide for compliance with a Remediation Plan.

8. Draft Common Frame of Reference (DCFR)