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POLICY BRIEF ON ESG Due Diligence in EU Product Rules

Integration of economic, social and governance due diligence criteria in product requirements, market incentives and the product passport

Our key recommendations

The forthcoming EU legislative Sustainable Products framework should ensure the following:

- **Existing environmental, social and governance (ESG) reporting frameworks such as the Taxonomy Regulation and the Corporate Sustainability Reporting Directive should evolve towards a more holistic view of sustainability.** The range of ESG impact indicators should be extended, particularly in the social and governance domain. The development of technical standards should already now consider the needs of a potential product-oriented framework with impact indicators, and not focus on minimum safeguards and due diligence only.

- **Product passports should build on this wide set of indicators to ensure a holistic approach to sustainability right from the start.** Companies should be incentivized to gather data and ultimately face product bans if they are not able to demonstrate that products do not negatively impact sustainability. In an initial phase, data at company level produced in the context of existing legislative obligations might be used as a proxy for data at product level.

- **Sustainability information in the product passport should cover the entire value chain.** There are several tools, including Social Life Cycle Assessment, that can be used by companies to identify risks across the entire value chain.

Introduction

The European Commission adopted the Circular Economy Action Plan in March 2020, and is currently preparing its Sustainable Products Initiative, to make goods and services "*fit for a climate neutral, resource efficient and circular economy, reduce waste and ensure that the performance of frontrunners in sustainability progressively becomes the norm*."[1] The Sustainable Products Initiative might include due diligence, market incentives and possibly a product passport for a much wider group of products than currently covered by the Ecodesign Directive. It is expected to include "*social aspects throughout the product lifecycle as part of the sustainability principles and requirements*"[2].

This paper sets out how social and environmental due diligence criteria can best be integrated in the sustainable products initiative, to ensure that not only companies, but also individual products are subject to sustainability due diligence requirements and that sustainable products progressively become the norm, rather than the exception.

1. Product due diligence – why does it matter?

Improving sustainability and transparency

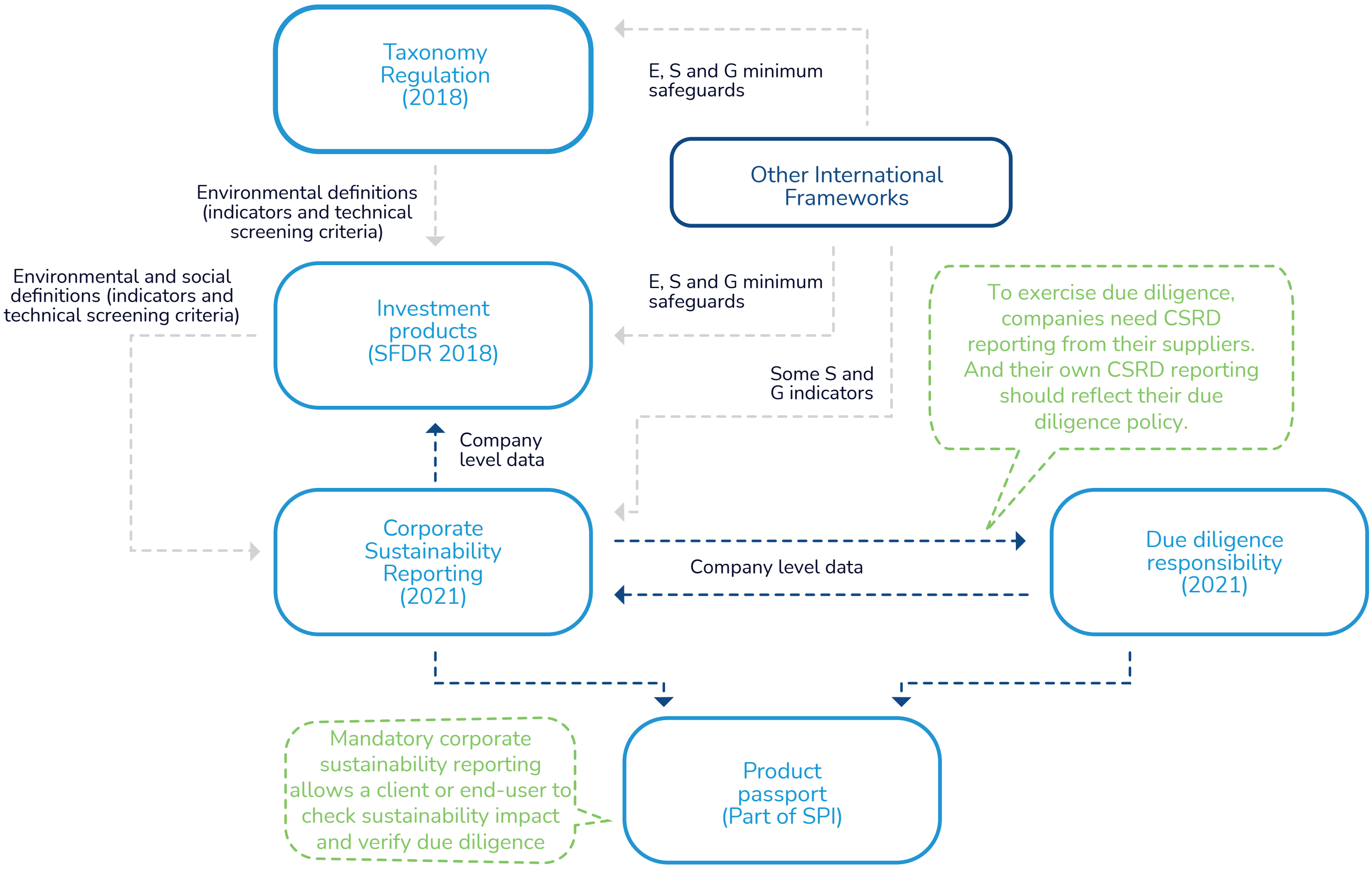
European citizens and consumers are increasingly concerned about the environmental and social impact of the products and services they buy . This puts companies under pressure to better understand, integrate and disclose the negative externalities of their business models, including in the field of social and environmental impacts. Examples of such externalities include greenhouse gas emissions and biodiversity loss in the environmental domain, and non-respect for workers' rights, child labour and human rights abuses in the social domain.

To prevent greenwashing and to ensure fair competition in the internal market, the EU has started to adopt legislation to improve transparency on corporate sustainability, with an initial focus on positive impact in the climate field, given the momentum on climate action following the 2015 Paris Agreement. Two legislative initiatives adopted as part of the Sustainable Finance Action Plan launched in 2018 aim to improve transparency on the sustainability impact of corporate activities (Taxonomy Regulation) and financial investment products (Sustainable Finance Disclosure Regulation), so that companies and consumers can make more sustainable choices.

The Taxonomy regulation focuses on activities that have a positive impact on indicators related to six environmental objectives. It takes a much less ambitious approach of merely respecting minimum international safeguards on social and governance issues (see infographic). The Sustainable Finance Disclosure Regulation adds a few high-level social positive impact indicators and builds on the Taxonomy's six environmental objectives. Sustainability must be considered in a more holistic way and fully include the social and governance dimensions of sustainability. This could also include the disclosure of the sustainability impact of individual products in a product passport.

Furthermore, transparency on sustainability should only be a first step, to be followed by minimum product requirements. In product regulation, the EU has indeed moved further and adopted legislation that effectively bans the worst performing products from the common market, such as certain light bulbs and vacuum cleaners under the Ecodesign rules. The EU represents one of the largest markets in the world and can use its market power[4] to define a global minimum sustainability standard for products. This could include rules[5] that ban products from the internal market that do not meet a given minimum sustainability standards, including on a wide set of Environmental, Social and Governance (ESG) indicators.

How a product passport could build on existing EU sustainability transparency legislation



What is due diligence?

Over the past years, European policy-makers have started to pay greater attention to the concept of corporate due diligence, "the processes through which enterprises identify, prevent, mitigate and account for how they address their actual and potential adverse impacts" as defined by the OECD[6].

Due diligence has gained special prominence in EU and European national legislation in the past years. Several EU Member States have introduced national due diligence legislation, expecting businesses to identify potential negative sustainability impacts in their supply chain and take responsibility for mitigating these impacts. Generally, due diligence legislation is embedded in company law and seeks to ensure that large companies within a jurisdiction or active on the market in that jurisdiction disclose and implement a due diligence policy. The national models in European countries vary greatly in terms of the types of issues that are covered by the legislation[7] but usually include human rights and environmental impacts. Other social issues, such as "modern slavery" (UK) and child labour (Netherlands) have been the subject of specific national legislation.

At the EU level, political momentum has in particular been building up since the implementation of the "duty of vigilance" legislation in France in 2017. At the same time, other political trends such as the increased awareness of climate change (since the Paris Agreement in 2015) and improved corporate transparency (Non-Financial Reporting Directive, 2014) have increased pressure on managers to better integrate the societal impacts of their corporate activity in decision-making.

The EU due diligence framework, planned for the autumn of 2021, is expected to focus on preventing the negative impact of corporate activities and their products by requiring companies to take ownership and accept responsibility and liability for their supply chains. The framework will most likely strongly rely on the concept of Environmental, Social, and Governance (ESG) factors as commonly used in the field of financial investments and defined by the 2006 United Nations Principles for Responsible Investment[8]. This framework consists of three pillars of sustainability: environmental issues, social issues including human rights, and corporate governance issues, all of which are understood to influence the sustainability of a company and its products and services.

Applying due diligence to products

By applying the company-level due diligence framework that is currently being developed to the field of product regulation, the EU can create a basis for the promotion of sustainable products over non-sustainable ones, including through the introduction of minimum thresholds that will effectively take the worst-performing products off the market.[9]

For such strategies to work, the disclosure framework must include <u>indicators at product level</u>, based on an <u>enlarged set of sustainability indicators</u>, cascading all the way <u>down the supply chain</u>.

In this brief, we explain:

- how the EU's political process on due diligence can support the inclusion of environmental and social indicators relevant for individual products;
- how it can ensure that a wide range of sustainability concerns are taken on board, beyond those currently foreseen in EU legislation; and
- why reporting and due diligence legislation must account for the full product chain for product requirements to be effective.

2. Problem analysis

The European Union's future *corporate* due diligence and disclosure framework is a good basis for *corporate* due diligence. However, it is likely to miss certain features that are essential for an effective due diligence and disclosure framework for sustainable *products*.

Decision-makers need to address three dimensions of this problem:

A. The existing sustainability indicators and legislative initiatives focus on companies, not products

B. The range of sustainability indicators available in existing legislation is too limited

C. Product due diligence requires full supply chain responsibility and information

In this section, we discuss each of these three dimensions individually.

A. The existing sustainability indicators and legislative initiatives focus on companies, not products

From a political, timing and legal consistency perspective, any future due diligence product requirements in the context of the Sustainable Products Initiative should be linked to existing corporate sustainability and due diligence legislation wherever possible.

However, the two initiatives most relevant and subject to legislative negotiations at the moment, are both designed at company level and not at product level:

- the Corporate Sustainability Reporting Directive (CSRD), proposed by the European Commission in April 2021, revises the Non-Financial Reporting Directive adopted in 2014 and introduces a range of sustainability indicators on which large European companies and listed SMEs will have to report, together with their financial annual reporting obligations. Smaller non-listed SMEs are not bound by these mandatory rules and might publish such information only if pressured by their suppliers and financial partners.
- the forthcoming EU Due Diligence legislation, will impose due diligence obligations at company level. It relies on appropriate sustainability reporting including from the CSRD to ensure companies receive the sustainability information they need from their suppliers, so that they in turn can meet their due diligence obligations. The reporting will also allow supervisors and impacted third parties to enforce due diligence rules.

A major challenge is therefore to ensure that disclosure is sufficiently detailed at corporate activity level, so that the ESG indicators at corporate level can be used for product requirements, or preferably that separate disclosure of individual product sustainability is provided for. Without this information, it will be impossible to distinguish the sustainability impact of individual products from the same company. As an example, under the Sustainable Finance Taxonomy rules, a company building railway stock is considered very sustainable based on its sector code (based on the EU Nomenclature of Economic Activities – NACE), but its products might have a very divergent sustainability profile: an electric train likely to operate at maximum capacity with passengers who would otherwise drive or fly, is probably far more sustainable than a diesel train that is planned to be used to transport coal to a power plant.

B. The range of sustainability indicators available in existing legislation is too limited

At the moment there is no full detailed set of indicators on all environmental, social and governance issues in EU legislation that sustainable product rules could refer to. We discuss the frameworks that do provide some indicators but not a full range of sustainability issues.

The sustainability indicators in the Corporate Sustainability Reporting are to a large extent based on the Sustainable Finance Taxonomy Regulation (see infographic).

The Taxonomy Regulation defines six environmental “objectives” and related indicators for an activity to be considered as positively contributing to that objective. It does not define the thresholds for those indicators; these thresholds are part of the “technical screening criteria” established by the European Commission in a delegated process, with input from the Platform on Sustainable Finance. The Taxonomy also does not distinguish between activities that are “neutral” or “negative” in terms of contributing to one of the six objectives, as it was never intended to do so – its stated purpose is to *stimulate* environmentally sustainable investments and not necessarily to rate all corporate activities on a sustainability scale.

As regards the social and governance-related side of sustainability, the Taxonomy is limited and only defines minimum safeguards based on international standards that should be respected. This is not sufficient to provide an assessment of the sustainability of corporate activities (or products at a later stage), as such an assessment would also require defining positive impact indicators and related thresholds in the social and governance domains. While initiatives are being taken to expand the Taxonomy to include social and governance objectives, this is a long-term process, both at the political and technical level.

The CSRD builds on the Taxonomy and takes a first step to extend ESG reporting with some new social and governance “factors”. However, the indicators as announced (see infographic) are limited and some continue to take a “minimum safeguard” perspective, such as “respect for human rights and international conventions”[10]. Such indicators might be helpful to cover the “negative” side of sustainability (preventing harm) and allow companies subject to the forthcoming corporate due diligence rules to get the appropriate reporting from their suppliers. It will however not be sufficient to allow companies to disclose the sustainability *impact* of their business and individual products. Preventing harm, respecting working conditions or human rights when running a business does not guarantee that any or all of the products made by that business are providing a significant positive *contribution* to sustainability – they could be relatively neutral to such objectives as well.

The indicators to be developed as part of the CSRD are being elaborated in parallel to the legislative negotiations on the CSRD and should be completed in two sets by October 2022 and October 2023, respectively. The political and technical design of this sustainability reporting framework should ideally consider the future needs of a potential product passport framework, including the need for positive impact indicators, to avoid another iteration in the process of defining indicators and thresholds if and when the EU adopts product information requirements.

ESG reporting scope of the Corporate Sustainability Reporting Directive and existing legislation

C.Product due diligence requires full supply chain responsibility and information

In the context of due diligence requirements, a third key political and technical challenge is to ensure that the full supply chain is covered. Companies claim high difficulties and costs to identify their full supply chain[11], and often indicate a preference for a cascaded system where they only take responsibility for their direct suppliers ("Tier 1"). Industry representatives also indicate that some supply chains are quite long, with many intermediaries along the way (e.g., the textile supply chain consists of 12 steps in some cases[12]), or that in shorter supply chains there are many inputs into one single product that is placed on the EU market (e.g., a mobile phone consisting of thousands of components).

Some companies claim that it is impossible to have legal certainty regarding where their suppliers claim raw materials and intermediate products are sourced from. In their view[13], it is unfair to impose corporate liability without a global framework requiring global suppliers to *disclose* what takes place in the supply chain, so that they can hold their suppliers accountable.

However, for sustainable products to become the norm, product manufacturers cannot ignore parts of their supply chain and must identify and disclose the sustainability impacts of the entire chain. Every step in the process must be documented and information must be passed on along the value chain, so that the final party can understand the sustainability impact of their products. Technical and legal solutions could be designed to help companies to take responsibility and liability for their entire supply chain and enforce that responsibility.

3. Effective measures to address the issue

In this chapter, we build on the problem analysis and consider measures and inspiring policy initiatives that could help define policy on product due diligence, for each of the three problem dimensions.

A. Including product-related indicators in the sustainability reporting frameworks

Since the publication of the Timber Regulation[14] well over a decade ago, political support is growing for measures that impose sector-specific due diligence requirements for products from high-risk sectors that are placed on the EU internal market. The Sustainable Products Initiative could build on these sector-specific rules and extend them to product groups for which there is consensus that they are high-risk from an environmental, social and/or governance perspective.

The Commission's Inception Impact Assessment on the Sustainable Products Initiative provides some guidance as regards the product groups that could be prioritised: electronics, ICT, textile, furniture, steel, cement and chemicals. Politically, it will be helpful if the Commission includes all these product groups in its legislative proposals as part of the Sustainable Products Initiative.

Existing legislation provides some guidance as regards the indicators that could be relevant across these product groups. This includes the indicators listed in the Timber Regulation covering solid wood products, flooring, plywood, pulp, paper etc., such as **detailed geographical information** on all raw materials and parts, **information on all suppliers** and traders and **risk assessment procedures** (in the framework of the Sustainable Products Initiative these should be ESG risk assessment procedures). The Conflict Minerals Regulation[15] can be a supplementary source of inspiration: importers of tin, tantalum, tungsten and gold are obliged to keep detailed information on **suppliers**, **traders**, **areas** and **time of extraction**.

An ambitious legislative proposal on Sustainable Products should build on and be compatible with the existing product-level reporting for minerals and timber products, and also include indicators relevant to products covered by the Commission's textile strategy and the forthcoming legislative proposal on deforestation and forest degradation[16].

The first building block of this process is the elaboration of the main themes around which ESG indicators should be constructed. As for the environmental indicators, the six environmental objectives of the Taxonomy Regulation and the related technical criteria contained in the draft delegated act are relatively stable and can be applied for use[17].

There are however two main challenges:

1. The criteria used in the Taxonomy need to be re-formulated as outlined above to move their focus from economic activities to products and allow for product-level disclosure in addition to company level disclosure. For reasons of legal consistency, this should not be done in the main legislative text on Sustainable Products but in a delegated act stemming from it. This will only happen if the legislative text provides a clear mandate for such an exercise.

2. To enable future bans on products with a manifestly negative impact, the indicators should be expanded to define positive, neutral and negative contributions to the sustainability objectives, not just positive impact as is currently the case. For environmental indicators, the current "do not significant harm" threshold could be a starting point to define the threshold between neutral and negative.

The second building block of effective product-level reporting is a system that acts as a sufficient deterrent to non-compliance. This could include the establishment of an obligation for Member States to conduct official checks on the premises of operators and field audits by competent authorities or independent verification bodies (including in third countries; see example below on the Ship Recycling Regulation) to verify the soundness of product reports and adopt sanctions such as fines and then provisional or permanent product bans. To further guarantee effective enforcement of the new legislation, consumers, workers and impacted communities from all over the world should have the right to seek redress before EU courts, in particular when it comes to human rights violations.

B. Moving towards a holistic view of sustainability

During the legislative negotiations on the Sustainable Finance Taxonomy Regulation, one of the issues on the table was the expansion of the taxonomy beyond the six proposed environmental objectives, to social, governance and additional environmental objectives. As part of the negotiations, the European Parliament produced a compromise text[18] (see textbox) which proposed to extend the taxonomy to social issues, listing the indicators that should form part of a social taxonomy in amendments. While MEPs ultimately decided to request the Commission to present a proposal at a later stage, the list is a helpful consolidated overview of the objectives that should be considered fundamental to social sustainability.

The European Commission's proposal for a Corporate Sustainability Reporting Directive puts forward a set of three social objectives: "equal oppor-

European Parliament proposed compromise amendment on social objectives in the Taxonomy Regulation, based on amendments 494-497

1. An economic activity shall be considered to contribute substantially to social objectives through any of the following means:

(a) promoting equitable access to affordable, safe, sufficient and nutritious food and/or ensuring food security;
(b) promoting equitable access to health services and universal health coverage;
(c) promoting equitable access to education and training;
(d) promoting equitable access to social protection;
(e) promoting equitable access to adequate and affordable housing;
(f) promoting equitable access to essential basic services, including water, sanitation, energy, transport, financial services and digital communication; and
(g) supporting the development of social economy organizations and social enterprises

tunities"; "working opportunities" built on the European Pillar of Social Rights; and human rights.

Under the "Pillar of Social Rights", objective 1 relies mostly on policy statements and refers to education and training, gender, racial, ethnic, religion or belief, disability, age or sexual orientation equality. Objective 2 has more easily quantifiable safeguards and includes decent wages, dismissal protection, social dialogue and health protection[19]. A reporting system obliging producers and importers to request this information from all their suppliers of raw materials and/or intermediate parts could lead to some kind of "social labelling" of the socially most responsible products, as well as a ban on products with no social tracing or that do not respect minimum standards: the more safeguards in place (decent wages or remuneration of independent suppliers, health protection, working time, social dialogue), the better score a product label will show.

The concrete labelling and minimum criteria should be spelled out in a delegated act taking different product realities into account. Products for which it is not possible to gather this information, should be excluded from the EU single market. Some features (a ban of child labour, the existence of some basic health and security measures; etc.) should be recognised as absolute safeguards and the inability to guarantee them should lead to product bans. Moving forward in this direction would concretise the spirit expressed in the EP Taxonomy Regulation amendments mentioned in the textbox above.

Other international frameworks also provide inspiration for measuring positive impact on wider aspects of sustainability, including the UN Sustainable Development Goals (SDGs)[20] as recognized by the Platform on Sustainable Finance which has a subgroup working on a potential social taxonomy[21].

Finally, the European Parliament amendments mentioned above also proposed a much wider set of international conventions that could be used as "minimum safeguards":

- the International Labour Organisation's (ILO) declaration on Fundamental Rights and Principles at Work and the eight ILO core conventions;
- the International Bill of Human Rights, the EU Charter of Fundamental Rights;
- the United Nations Declaration on the Rights of Indigenous Peoples (UNDRIP);
- the UN Convention Concerning the Protection of the World Cultural and Natural Heritage;
- the UN Guiding Principles on Business and Human Rights;
- the UN Principles for Responsible Investment;
- the OECD Guidelines on Multinational Enterprises; and
- the OECD Due Diligence Guidance for Responsible Business Conduct.

While useful as a conceptual starting point, these minimum standards ultimately need to be developed into impact indicators, because due diligence standards are typically risk-based and ask companies to focus on high-risk issues, sectors, suppliers, or geographies. If reporting only covers the most severe impacts, no data will be available on other or less significant impacts.

We note that some of the indicators and safeguards above are hard to quantify; beyond identifying which social issues are salient, it therefore also makes sense to support policy initiatives that aim to quantify social and governance indicators, or at the very least to determine which indicators can be relatively easily mapped to be used in product policy or for market incentives. In line with the proposal of the Commission on sustainability reporting (CSRD), this task could be given to EU agencies or other advisory bodies in the legislative negotiations on the Sustainable Product Initiative, subject to appropriate checks and balances in terms of industry and non-industry composition of any advisory groups.

Despite the challenges, the initiatives discussed demonstrate the momentum for moving to a wider set of ESG indicators and provide helpful inspiration for defining what a list of social impact indicators and safeguards would look like.

C. Helping companies meet full supply chain due diligence responsibilities, and/or technical product-level traceability tools

Provided that the right social impact indicators have been defined, the scoring on those indicators still needs to travel along the value chain in a reliable an efficient way.

One of the suggested measures in the Sustainable Products Initiative to address this challenge is to establish “EU rules for setting requirements on mandatory sustainability labelling and/or disclosure of information to market actors along value chains in the form of a digital product passport”. Such a product passport would integrate social and environmental due diligence aspects and enable a continuous flow of information allowing companies to effectively track their supply chains. It would be supporting companies in performing periodical and punctual checks related to human rights and environmental risks in the entire chain. As a tool, it could lead to a paradigm shift as regards sustainability product requirements. Companies are already carrying out meticulous checks on the *quality* of supplied product. To a certain extent, the very same quality controls and *processes* could be applied to due diligence processes, helping companies to inspect their value chains beyond Tier 1 suppliers.

Some EU companies might have difficulties getting the necessary data from their suppliers to meet the product passport requirements. However, the very act of imposing a product passport requirement on EU companies will trigger the development of reporting standards and will force non-EU companies to comply with the product passport rules if they want to continue exporting to the EU. Alternatively, intermediaries might start to propose compliance services for companies wanting to export their products to EU companies. This is a mechanism observed in financial services, where investment product issuers under new EU SFDR legislation are obliged to report on the sustainability of their investment products, which in turn triggers the supply of data from investee companies and has accelerated the development of a market for sustainability data.

In the framework of the upcoming Sustainable Product Initiative, there are several tools which could be considered to support companies in meeting their due diligence obligations, including:

- Support for applying a **Social Life Cycle Assessment** (S-LCA) methodology, which is gaining momentum among stakeholders, business representatives and policy makers, and could prove to be an essential instrument in the assessment of products' social impacts[22]. The methodology building on the traditional Environmental Life Cycle Assessment could be applied to assess the actual or potential social impacts of a product across its life cycle. The S-LCA could serve as a tool to perform the value chain social risk assessment and identify actual or potential social impacts within a production cycle. If carried out together with Environmental Life Cycle Assessment, it helps to understand a broad range of sustainability impacts with a product.

- Using **blockchain technology** to ensure information on the product at various stages in the value chain is unchangeable and can be publicly verified; the entire blockchain can also be made transparent to the end user through technology such as QR codes.

- Imposing a system of **"cascaded" supplier management** building on standards such as ISO 9001 (quality management systems). This standard encourages suppliers to also be ISO 9001 compliant and ultimately could mean companies can only (source from) companies that themselves meet the standard's requirements, creating a chain of trust along the value chain. This is a solution that strongly relies on process commitments and depends on credible commitment and enforcement to have an effect.

- **Spot checks**, as a stopgap measure to ensure sustainability information from non-EU suppliers is verified. The EU could consider creating a system of mandatory occasional spot checks in the value chain, including in third countries, as part of corporate due diligence policy. Such a model is implemented in the Ship Recycling Regulation, where EU firms must have independent spot checks[23] conducted on non-EU sites where old EU ships are processed; third country sites have a strong commercial interest in ensuring that European ships can be dismantled and recycled there because of the significance of the EU market, and therefore voluntarily submit themselves to EU supervision and site inspections.

4. Concrete recommendations to be inserted in EU sustainable product policy

Based on the previous problem analysis and inspiring policy initiatives, the following suggestions could be integrated into the Sustainable Product Initiative (SPI):

1. The initiative should encompass the **full set of aspects determining the sustainability of a product**. The focus should not only be on environmental impacts, but increased attention should be paid to social and governance impacts, to adopt a holistic approach to sustainability.

Significant efforts will be needed to develop **more extensive range of indicators**, especially the social and governance side. In this context, inspiration could be taken from the EU Taxonomy Regulation, the Conflict Minerals Regulation, the EU Timber Regulation and other legal instruments such as the Pillar of Social Rights.

There are **different ways** to introduce more detailed sustainability indicators, including by amending the CSRD to ensure a wider set of indicators is available than strictly needed from a corporate reporting or sustainable finance perspective. Alternatively, the Sustainable Products Initiative could also impose direct and separate disclosure requirements.

In either case, the SPI should also ensure that the parallel **"technical" process** in which the European Standard Setter (currently EFRAG, the European Financial Reporting Advisory Group) advises the Commission on the definition of sustainability indicators is adapted to take into account the needs of the Sustainable Product Initiatives and includes stakeholders with knowledge of wider sustainability issues and representatives relevant for product-related disclosures.

2.The product-specific indicators should subsequently serve as the **basis for product passports**. On the environmental side, such product passports should include information about CO2 emissions, the use of hazardous substances and waste generation during the production and transport of all parts, but also information about the durability, repairability (when applicable) and recyclability of the final product in line with the Taxonomy Regulation's six objectives and technical screening criteria. Concerning social aspects, information such as on workplace safety, decent wages, health and social insurance coverage and the existence of social dialogue structures between employers and trade unions should also be included in the product passport.

In order to encourage EU companies to **develop sustainability assessment capacity**, the EU could ultimately consider product bans in case there is an inability to demonstrate that all social safeguards are in place for every raw material and part used in a product.

For sectors where no sector-specific product sustainability indicators are available, **company-level data** could be considered as a proxy for product-level data, potentially during a transition phase only. This is suboptimal, because company-level data is likely to be focused on respect for minimum safeguards only instead of measuring (positive) sustainability impact. If a company respects minimum safeguards for all its products, each individual product will also comply with the safeguards. However, to measure positive sustainability impact it is not possible to use company-level data as a proxy, as it is not possible to measure to what extent individual products contribute to the positive sustainability impact. The Sustainable Products Initiative needs to introduce product-level disclosure requirements to measure such impact.

3.It is essential that the sustainability information included in the digital product passport covers **the entire value chain**, as otherwise important information about social and environmental risks will be lost. Social and environmental life cycle assessment methodologies could play a major role in enabling the evaluation of social and environmental impacts along the value chain. More specifically, the Social Life Cycle Assessment methodology could support the identification of "social hotspots" in specific sectors, providing companies guidance on which impacts to prioritise in their product information disclosures.

As part of full chain visibility and responsibility, the forthcoming Sustainable Product Initiative should have adequate **enforcement measures**. The reliability and correctness of the provided sustainability information has to be verified by national competent authorities and/or independent auditors on a regular basis, to ensure the functioning of the whole product passport system.

5. Expected impact

A **more holistic view of sustainability** will benefit society as a whole, as negative externalities related to unsustainable forms of production are avoided or better integrated into the transfer price of products along the value chain and in the end price of products on the EU market. This financially discourages practices that have a negative impact on sustainability. Such expected impacts are echoed in the Commission's Inception Impact Assessment, which describes the transition path towards making sustainable products the norm: initial higher costs related to better information and increased sustainability, will over time fade as the economies of scale for more sustainable products appear and the additional costs become marginal.

Moving **from company to product transparency** will allow end-users to choose more sustainable products and prevent greenwashing, as companies can no longer mix supply chains but must provide an overview of sustainability impacts across their product range.

The **inclusion of the entire value chain** will ensure that EU companies can compete on a fair basis with non-EU companies and avoids the displacement of production of products with a non-sustainable footprint from the EU to elsewhere (if imported "lack of sustainability" would not be addressed).

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EC register for interest representatives:
Identification number 06798511314-27
BCE identification number: 0415.814.848
RPM Tribunal de l'entreprise
francophone de Bruxelles

Published June 2021
Responsible editor: EEB
Authors:
Joost Mulder
Isabella Ritter
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With the support of the LIFE Programme of the European Union, Laudes foundation and the MAVA foundation. This brief reflects the authors' views and does not necessarily reflect the views of the donors.

This document was prepared by Better Europe for the European Environmental Bureau. The views expressed in this document are solely those of the authors and do not necessarily reflect the position of the EEB.